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TO PROVIDE REVENUE FOR WAR PURPOSES

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE UNITED STATES SENATE

SIXTY-FIFTH CONGRESS

SECOND SESSION

ON

H. R. 12863

TO PROVIDE REVENUE, AND FOR OTHER PURPOSES

—

Printed for the use of the Committee on Finance



WASHINGTON
PRINTING OFFICE

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TO PROVIDE REVENUE FOR WAR PURPOSES.

FRIDAY, SEPTEMBER 6, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to call, at 10 o'clock a. m. in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present: Senators Simmons (chairman), Williams, Smith, Thomas, Gore, Jones, Nugent, Penrose, Lodge, McCumber, Smoot, Townsend, and Dillingham.

The committee proceeded to the consideration of the bill (H. R. 11283) "to provide revenue and for other purposes."

The CHAIRMAN. Gentlemen of the committee, we have a majority here, and the committee is ready to proceed with hearings. It is proper that I should state that, of course, it is understood that the bill has not yet been acted upon by the House, and we have not jurisdiction of the bill. But in order to facilitate its consideration we have decided to have hearings while the House is considering the bill, so that as soon as it comes over and is reported to the Senate and referred to the committee we may proceed with the consideration of the bill.

Senator SMOOT. As the bill may be reported.

The CHAIRMAN. As the bill may be reported. We are simply assuming for the present that the House will pass the bill as it has been reported to it by the Ways and Means Committee.

Senator LODGE. Substantially.

The CHAIRMAN. Substantially; yes. It is also proper that I should state that the committee decided, in ordering these hearings, that we would give at least a week's hearing—not more than 10 days—and in order that the hearings may be concluded within that limited period of time the committee decided to ask the several industries which may wish to make statements to the committee to select some representative of the industry to present their case orally, with the understanding that any briefs that the representatives of the industry may wish to file can be filed and printed along with the oral hearing.

MAIL-ORDER HOUSES.

Senator SMOOT. I will say to the chairman that I asked the gentleman representing the mail-order houses if he would not be here this morning to begin at once, and he said that he desired to leave as quickly as possible, so I told him he would be heard the first thing this morning, so I ask that Mr. Eiswald be heard first.

The CHAIRMAN. You may proceed, Mr. Eiswald.

**STATEMENT OF MR. G. H. EISWALD, PRESIDENT OF THE
CHARLES WILLIAM STORES (INC.), NEW YORK.**

Mr. EISWALD. The statement I will make to the committee is submitted by the following:

J. I. Zook, treasurer, Montgomery Ward & Co., Chicago.

S. G. Rosenbaum, president, the National Cloak & Suit Co., New York.

W. R. Heath, vice president, the Larkin Co., of Buffalo.

G. H. Eiswald, president, the Charles William Stores, New York.

Milton Cone, president, the Spotless Co., Richmond, Va.

These gentlemen represent their respective corporations, and in addition the majority of the so-called mail-order houses of the United States.

Our subject is a tax of 1 per cent on sales by mail, proposed in the revenue bill now under consideration by the Senate Finance Committee, to wit [reading]:

SEC. 1005. That on and after January first, nineteen hundred and nineteen, every person, any part of whose business consists of the retailing of merchandise through or upon orders received by mail, shall pay annually a special excise tax equivalent to one per centum of the gross amount in excess of \$100,000 received by such person from such retail sales during the preceding year ending June thirtieth.

The necessity for revenue by the Government is recognized, and every just and fair method of producing it will meet with our hearty approval and assistance.

We offer no objection to a tax of 1 per cent on sales as a tax, provided it is levied on all sales, irrespective of the way in which they are made. Such a tax is just, moderate, easy of determination and collection, and, if applied to all sales, would yield enormous revenue. If applied to sales by mail only it would yield at the most a relatively small amount.

In passing, we wish to direct your attention without further comment to the ambiguity of the section under consideration.

Senator PENROSE. Did you present these views to the Ways and Means Committee?

Mr. EISWALD. Substantially, Senator.

Senator PENROSE. And they overruled your objections?

Mr. EISWALD. The Ways and Means Committee appointed a subcommittee to hear our case, and the subcommittee, consisting of five members, reported unanimously in favor of reconsideration of this clause. But the Ways and Means Committee as a whole, I am told, overruled the recommendation of their subcommittee.

The language of this bill is open to various interpretations, entirely irreconcilable with justice and inviting controversy and litigation, and possibly leading to great difficulty of administration.

It is apparent that the great bulk of the revenue received by the Government from this source will be from so-called mail-order houses and those large retail establishments who invite orders by mail.

We list herewith all of the retail mail-order houses in the United States of which we have any knowledge, and have placed opposite their names the amount of business which they did for the calendar year ending December 31, 1917.

In the case of those houses marked (a) the figures are taken from official reports which are a matter of public record.

In the case of those houses marked (b) the figures are from information given us by the respective chief executives of the houses in question.

In the case of those marked (3) the figures are generously estimated.

(a) Sears, Roebuck & Co., Chicago, Ill.	\$165,807,608
(a) Montgomery Ward & Co., Chicago, Ill.	73,512,645
(a) National Cloak & Suit Co., New York	27,649,537
(c) Larkin Co., Buffalo, N. Y.	20,000,000
(b) Charles William Stores, New York	19,533,000
(b) Bellas Hess & Co., New York	12,000,000
(c) Hartman Furniture & Carpet Co., Chicago	8,000,000
(c) Spiegel-May-Stern Co., Chicago, Ill.	6,000,000
(c) The Catalogue House (Phillipsborn), Chicago, Ill.	5,500,000
(c) M. W. Savage Factories, Minneapolis	5,000,000
(c) The Wm. Galloway Co., Waterloo, Iowa	4,000,000
(b) Standard Mail Order Co., New York	4,000,000
(c) Straus & Schram, Chicago, Ill.	3,000,000
(c) Pacific Coast Mail Order Co., Los Angeles, Cal.	3,000,000
(c) Chicago Mail Order Co., Chicago, Ill.	1,750,000
(b) Perry Dame & Co., New York	1,514,000
(c) Cussins & Fearn, Columbus, Ohio	750,000
(b) Spotless Co., Richmond, Va.	600,000
(c) Harris Bros., Chicago, Ill.	500,000
(c) Crofts & Reid, Chicago, Ill.	500,000
(c) Hamilton Garment Co., New York	250,000
(c) Knickerbocker Mail Order Co., New York	250,000
Total	363,117,276

In addition to these houses there are a number of department and specialty stores who do more than \$100,000 of business by mail. These concerns, such as—

Marshall Field & Co., Chicago, Ill.	B. Altman & Co., New York.
The Fair, Chicago, Ill.	Best & Co., New York.
The Boston Store, Chicago, Ill.	Stern Bros., New York.
Carson, Pirie & Scott, Chicago, Ill.	Bedell & Co., New York.
John Wanamaker, Philadelphia and New York.	Jordan Marsh & Co., Boston, Mass.
Franklin Simon & Co., New York.	Weinstock, Lublin & Co., Sacramento, Cal.

and others, are not generally known as mail-order houses and only a small percentage of their business is done by mail.

Also there are some houses, such as seed distributors, nurserymen, and manufacturers of wire fences, stock foods, bicycles, windmills, household ranges, kitchen utensils, agricultural implements, etc., who sell their specialties at retail by mail. It is estimated that the total mail order sales of all the classes of business mentioned in this and the preceding paragraph are not in excess of \$50,000,000 or \$60,000,000.

It will be seen from the foregoing figures that the total mail-order business of the United States is very likely not in excess of \$425,000,000. Therefore, a tax of 1 per cent on sales would not yield more than \$4,250,000 of annual revenue. This sum we consider a generous maximum, and furthermore, this tax would so reduce the profits of business houses that the excess-profits tax which many of them pay would also be reduced.

In some of the larger houses it is figured that their net payment on tax would be reduced by 20 per cent as a result of the

imposition of this 1 per cent sales tax. Instead of yielding the Government an increased revenue of \$4,250,000, it is doubtful whether the net revenue to the Government on account of this tax would be in excess of \$3,500,000.

The business popularly called the mail-order business is a retail business. It consists of marketing merchandise of various kinds directly from factory to consumer, eliminating the jobber and middleman. It sells groceries and provisions, clothing, dry goods, agricultural implements, occupational tools, household articles, and other goods for the farm and home. Its customers are principally farmers, mechanics, laborers, and people living in the villages and small towns where shopping facilities are limited. Mail-order houses do very little business in the larger towns and cities where shopping facilities are good, but do provide the people living in the country districts and small towns with the ample assortments and lower prices that can usually be obtained only in the large cities.

Its method of sale involves the use of the United States mail instead of the use of sales people or stores.

The mail-order business does not enjoy any special or unusual postal privilege or franchise of any sort. On the contrary, most mail-order houses, in order to facilitate the handling of their letters, catalogues and parcels, do at their own expense a great deal of sorting, routing, bagging, and carting, thus relieving the Post Office Department of much work which it is required to perform for the smaller users of the mails.

The Post Office Department generally, from expressions which we have heard, regard the mail-order business as profitable to them, a business easy to handle on account of its large volume and unity.

The mail-order business, generally speaking, is done on a high plane. All mail-order houses of which we have any knowledge do business upon the basis of refunding the money to the customer, together with all transportation charges, for any goods which are not satisfactory. The mail-order concerns are nationally famous for their efficient methods of administration. The whole business has been developed by supplying its customers with reliable merchandise at substantial savings.

The mail-order business performs a great economic function by keeping prices down to a lower margin of profit and stimulating competition—

Senator THOMAS. Are they doing any business in the District of Columbia?

Mr. EISWALD. Very little, I am sorry to say.

The mail-order business performs a great economic function by keeping prices down to a lower margin of profit and stimulating competition, thus directly benefiting the people living in the country and small towns. The country merchant regards the mail-order catalogue as the great price maker.

We wish to quote from a letter written to Congressman H. B. Flood, on August 30, 1918, by Mr. A. B. Thornhill, president of a large farmers' grange, with 20,000 members in the State of Virginia alone (reading):

I am writing to call your attention to the fact that the mail-order houses sell nearly all of their goods to the farmers in the rural districts, and very little

or any goes to the city consumers. The organized farmers of our State have a contract with the Spotless Co., in Richmond, a mail-order house, and we have found it the only lever we had to keep down the retail prices under the existing circumstances.

The retail merchants' association is so well organized that it is hard to tell just what the country people would pay for their goods except for this competition.

If this tax could be extended to all business alike, then it would not be a hardship on any one class.

We contend that the savings made by our customers through their dealings with us enables them to accumulate property and, therefore, we are a substantial factor in aiding to build up the communities in which they live.

We offer no objection to any tax that is not discriminatory, but we wish to point out that this proposed tax, if constitutional, will be class legislation, punitive in its effect and meager in its results. It proposes to tax a very small group of business concerns, apparently, because they secure their orders through one of the great governmental agencies—the United States mail. It does not tax an article sold to a customer who makes use of the railroads or trolleys for the purpose of calling at a store in person to make his purchases; it does not tax the purchase made by telegraph or telephone; it does tax the purchase that is made through the mail. It means that a bill of groceries sold over the telephone or by means of the telegraph goes free, while the same order sent in by mail is taxed. It means that a shirt or plow sold by mail must bear a tax of 1 per cent, while a shirt or plow sold over the counter or by a salesman goes free.

Senator THOMAS. Is that entirely true? We have a tax on telephone messages, except local messages, and we also have a tax on all telegraph messages.

Mr. EISWALD. The sale goes free.

Senator LODGE. And there is also an added tax on letters.

Senator THOMAS. And also, as the Senator from Massachusetts suggests, an added tax on letters.

Senator McCUMBER. That is not a tax on the sale.

Senator THOMAS. No; it is not a tax on sales, but it is a tax upon the transaction.

Mr. EISWALD. We believe this is just as consistent as proposing to tax the manufacturer who uses water power in his business, and not one who uses steam. It is similar to a proposition to tax a self-service restaurant, the automatic style, and not a restaurant which employs waiters.

Our Government seeks to bring the producer and the consumer closer together for the purpose of preventing profiteering and reducing the high cost of living. By what theory, therefore, are sales by mail to be taxed and other sales not? One merchant makes a sale over the counter or through a traveling representative, and his sale is approved. Another man makes a sale by means of a letter or a catalogue, and his sale is taxed.

A tax on the sales of mail-order business would not be a tax on property, or on profits, or on a commodity, but would be a tax on a method—in this case a method of selling merchandise—and therefore, would be a discrimination.

We wish to point out that this tax will, in many cases, be confiscatory, because there are a number of mail-order houses who have

made no profit during the year 1918. A tax on their gross sales, therefore, would be confiscation of part of their capital.

This tax is retroactive for 18 months; it proposes a tax on all mail sales made since July 1, 1917. The retroactive feature levies tribute on a few business houses and must be paid out of their capital. Although the Government must have immediate revenue, it can not, in fairness, and with proper regard for the conservation of business, resort to such punitive and throttling measures. A universal tax collected by revenue stamps on all sales would bring immediate and thereafter daily revenue.

There is perhaps no one agency which is so productive of profitable revenue to the Post Office Department as the mail-order business. through the payment of postage on its letters and its catalogues and other printed matter, the shipment of merchandise by parcel post, and through the creation of first-class mail, registered mail, and money-order business from its customers as a result of the distribution of its printed matter.

It is conservatively estimated that the amount of postal revenue produced by the mail-order houses within the scope of the proposed tax amounts to \$24,000,000 per annum. To discourage the business can not help but appreciably curtail this revenue of the Post Office Department.

It is claimed by a few that mail-order houses pay no local taxes at the points at which they deliver their goods. We submit to your committee that it is contrary to custom and to the spirit of our institutions to call upon a concern to pay taxes both at the point at which it carries its merchandise and at which it delivers it.

The farmer raises his wheat in Iowa and ships it to Chicago or Minneapolis to be sold. He pays taxes in Iowa and not in Illinois or Minnesota.

The cotton goods manufacturer weaves his cloth in North Carolina and sell it in Boston or Philadelphia. He pays taxes in North Carolina and not in Massachusetts or Pennsylvania.

The stockman raises horses in Ohio and sells them in New York State. He pays taxes in Ohio and not in New York.

The miner produces coal in Pennsylvania, Indiana, or West Virginia and ships it to every part of the United States. He pays taxes only at the point at which he produces his coal.

We state, furthermore, that mail-order houses not only pay taxes at the points at which they carry their various stocks, but also pay to the United States Government every tax so far assessed against every other retailer.

The selling of commodities by mail direct to the consumer gives to millions of our rural population the facilities of the cheap markets of the large cities; it provides them with the opportunity for selection from stocks infinitely larger than are carried by retailers in rural districts; it keeps prices down by maintaining a lower margin of profit; and it stimulates competition, thus insuring to consumers the lowest possible prices.

The mail-order business is one of the main agencies in aiding the farmer and the wage earner in the rural districts and small towns to keep down the ever-rising cost of living, and we submit to your committee that it would be an injustice both to the consumer and to business to place a discriminatory tax on this important factor in

the commercial organization of the United States. It is the prosperity of the whole community that is the guarantee of democracy.

The CHAIRMAN. In your argument you have made a statement that if this tax were generally imposed it would yield a great deal of revenue. Have you made any estimate?

Mr. EISWALD. I have striven, with other people, to estimate what it would bring, tried to make deductions from the clearing houses, but I am unable to make any suggestion at all. The retail sales of this country, speaking commercially, are about 20 billion dollars. I have never found any way of estimating those sales that are not strictly commercial.

The CHAIRMAN. You also said that practically all of these sales were made in the rural districts.

Mr. EISWALD. Yes, sir.

The CHAIRMAN. Have you any information which you can give the committee as to what proportion of the sales are made in the rural districts?

Mr. EISWALD. Between 85 and 90 per cent.

The CHAIRMAN. How did you arrive at that estimate?

Mr. EISWALD. It is customary with the mail-order houses to try to confine their circulation as much as possible to the rural districts, because we are better fitted to serve the rural population than the city population. Therefore we scan our customer lists very carefully, and we always receive reports from our customer-list departments as to the proportion of rural population represented on our books. By rural population we consider those customers who are in towns of under 2,500.

The CHAIRMAN. You also stated that the imposition of this tax upon the mail-order houses would diminish the tax to be paid in other ways.

Mr. EISWALD. Yes, sir.

The CHAIRMAN. Would there be any difficulty in the way of these mail-order houses adding to the price of their goods this 1 per cent, or what is the equivalent to 1 per cent?

Mr. EISWALD. No objection. According to the theory of all taxation it would be passed on to the consumer. We could not, however, pass on to the consumer the retroactive feature, which proposes to tax us for the past 18 months.

Senator THOMAS. If it would be passed on to the consumer, I am against it.

The CHAIRMAN. There would be no difficulty in their passing this tax on to the consumer—that is, as to the future tax?

Mr. EISWALD. No difficulty, except a trading difficulty, in this way: We would be obliged to add 1 per cent to our price, whereas our competitors, the retail dealers, would not be obliged to. But they would add 1 per cent, and take it as additional profit, not having to pay this tax.

The CHAIRMAN. The difficulty would only grow out of competition?

Mr. EISWALD. Yes, sir.

The CHAIRMAN. Do not these mail-order houses usually somewhat undersell?

Mr. EISWALD. As a general thing they do.

Senator THOMAS. Is it not your experience that when a tax we levy is passed on to the consumer something is always added to it, or most always?

Mr. EISWALD. That is my personal experience.

Senator THOMAS. And if you can pass this tax on to the consumer, it would probably be 2 cents to him eventually, instead of the 1 per cent to you?

Mr. EISWALD. Outside of the ethics of it, I do not think that competitive reasons would permit us to do that.

Senator THOMAS. I do not confine my question to your business.

Mr. EISWALD. I understand.

Senator THOMAS. But generally. Your business is like any other. It will pass all expenses to the consumer that it can, which is perfectly legitimate. But I think in the operation of the existing law a great many of these taxes are passed on to the consumer, but they are doubled at the same time, if not more than that, and if this is a tax that can be passed to the consumer—and you say it can—I confess I do not feel very friendly to it.

The CHAIRMAN. Have you any further statements to make to the committee?

Mr. EISWALD. That is all, Mr. Chairman.

The CHAIRMAN. We are much obliged to you.

Senator THOMAS. Before we hear from another witness, if it be the intention of the committee to limit this hearing to 10 days, we ought to place a limit on the amount of time which each speaker appearing before us may occupy. Personally, I am not in favor of a limitation. I think it is a vastly important matter.

The CHAIRMAN. I thought we might proceed in this way to-day, and then we could determine a little bit later whether it will be necessary to do that in order to finish in the time we have allowed ourselves.

Is there any other gentleman who desires to be heard on this particular subject? We will hear from Mr. Heath, representing the Larkin Co.

Is the Larkin Co. a mail-order house, Mr. Heath?

STATEMENT OF MR. WILLIAM R. HEATH, REPRESENTING THE LARKIN CO., OF BUFFALO.

Mr. HEATH. A so-called mail-order house. I speak simply to call the attention of the committee to a different method which seems to be covered by this provision, retailing of merchandise.

Our orders are received by mail. A large portion of our business, however, is received from what have been popularly called clubs of 10 women going out and soliciting orders, securing the orders, and sending them to us. We pay for those orders; therefore we are paying a commission for business, although the business is received by mail.

The CHAIRMAN. Is it not merely a system of advertising? If you did not adopt that method you would have to advertise.

Mr. HEATH. Not at all. We advertise as other mail-order houses do.

The CHAIRMAN. This is merely supplementary to your advertising system, is it not?

Mr. HEATH. It costs us more than the advertising. It costs us as much as is ordinarily paid, I presume, by other houses who secure business that way. This would seem, therefore, to tax our company double even what it does ordinary mail-order houses.

I do not understand what is meant by "retailing of merchandise through or upon orders received by mail." We receive our orders by mail. Are they to be taxed, no matter how the order is secured?

The CHAIRMAN. You will have to make your own interpretation of it, and proceed with the argument. We are not going, at this stage, to attempt to interpret it.

Mr. HEATH. I did not intend that as a question I wanted you to answer. I only wanted to state the question that is in our minds. The mail-order business is presumed to be a profitable business. Between June 20, 1917, and June 30, 1918, our latest figures, our company suffered a merchandising loss. If, therefore, we pay a 1 per cent tax upon our sales for that year, it will be taken out of capital, besides suffering a loss that was quite severe. I think that is all I care to say.

The CHAIRMAN. That has reference to the retroactive feature?

Mr. HEATH. Yes, sir.

The CHAIRMAN. And your point is that if that provision should remain in the bill, you would have no opportunity to pass this tax on to the purchaser, as you will have with future sales?

Mr. HEATH. No; and unless conditions improve, Mr. Chairman, we will have no opportunity to pass it on any way. We can not pass it on and be assured of getting orders. It is orders out of which we pay our taxes. We must compete.

The CHAIRMAN. You say unless conditions improve. Is the mail-order business not prosperous at this time?

Mr. HEATH. We had large contracts for goods that were curtailed by virtue of the war.

Senator SMITH. It is a question of obtaining goods rather than of selling them?

Mr. HEATH. We can not obtain the goods at all, and then there are delays incident to railroad service, and the difficulty of securing goods that we could sell, or selling goods that we could secure, which has very much crippled our business. And it seems to us that the discrimination is entirely unjustifiable.

The CHAIRMAN. If there is no one else who wishes to make a statement to the committee with reference to this particular subject, we will hear any other gentleman who may desire to present any matter to the committee.

I understand Senator Smith of Maryland has asked for some time.

BROKERS.

STATEMENT OF SENATOR JOHN W. SMITH, OF MARYLAND.

Senator SMITH. Mr. Chairman and gentlemen of the committee, the gentlemen who are here with me to-day, and to whom you kindly agreed to give a hearing, represent a class of brokers and bankers in most of the cities of the United States. They feel that the tax that has been levied upon them is unjust, and they want to make a statement of their case to you this morning. I bespeak for them your

favorable consideration. I will first present to you Mr. John Hinkley.

STATEMENT OF MR. JOHN HINKLEY, OF BALTIMORE, MD.

Mr. HINKLEY. Mr. Chairman and gentlemen of the committee, I propose to be very brief. The particular matters we wish to bring to the attention of the committee are the two sections of the bill bearing upon a special tax upon members of stock exchanges. They will be found in two sections, one on page 125, which is the section with regard to a 20 per cent tax on dues, which places members of the stock exchange in the same category as members of clubs and imposes a 20 per cent tax.

Senator THOMAS. Section 801.

Mr. HINKLEY. Section 801. That applies to clubs of all kinds where the dues are over \$10 a year; and also produce exchanges, boards of trade, or similar organizations "maintaining a place where produce or merchandise is sold, or to any stock exchange." That means a tax of 20 per cent on dues of members of a stock exchange, and also any produce exchange. It means if a man is a member of more than one exchange he has to pay that on the dues of each exchange.

The other section we are interested in is section 1001, on page 139, which provides for a flat tax of \$100 on brokers, and which also provides, in the last part, which is the part we think is most open to protest, a tax based on the market value of a seat on the exchange on a sliding scale. The provision to which I refer begins on the bottom of page 139 and provides for a tax on a seat the value of which is not more than \$2,000 of \$50; where the value is more than \$2,000 and not more than \$5,000, of \$100; and if the value is more than \$5,000, of \$150.

Senator THOMAS. Those are additional payments?

Mr. HINKLEY. Those are additional taxes; yes, sir.

Senator THOMAS. In addition to the \$100 mentioned?

Mr. HINKLEY. In addition to the \$100 flat tax. Take, for instance, the Baltimore Stock Exchange. They have dues of \$200. That imposes a tax of \$40 for the dues to the exchange. It imposes a flat tax for being a broker of \$100, and it imposes a special tax, based on the value of the seat in the exchange, which in the case of the Baltimore Exchange would be \$100 more. So that is \$240 coming under these three heads that a member of the Baltimore Stock Exchange would have to pay for carrying on his ordinary legitimate business.

I have a little brief here which I will hand to the gentlemen of the committee.

The CHAIRMAN. Do you mean that \$240 is taxes or part of it is fees he has to pay to the exchange?

Mr. HINKLEY. A tax on dues is proposed to be considered as a tax.

The CHAIRMAN. What I was asking you is, if in this \$240 you are including anything except the tax he has to pay to the Government? I asked that because you said something about a member having to pay a fee to the club of \$100.

Mr. HINKLEY. No; \$240 is what a member of the Baltimore Stock Exchange has to pay to the Government for the privilege of doing

business. The dues to the exchange are \$200 per annum, and that forms the basis for the 20 per cent tax, which makes \$40, and then there is a flat tax of \$100, and then there is the excise tax of \$100 based upon the value of the seat upon the exchange.

The point I have made is that there are three different taxes laid upon stock brokers in the worst possible times. They have suffered more from the war than any other class of people, and they have done more to aid the Government in floating the loans than any other class, and made more sacrifice and effort. The points I have made in my brief are six:

First. That the business of a stock broker is not of such a character as to justify being singled out for special taxation as a business.

The business of a stock broker is to bring together the buyer and the seller, and he trades under the rules of the exchange. Everything is public—of record. And he gets only a fixed commission for bringing the buyer and seller together.

A point that was suggested to me by the argument just made before the committee is that there is no possible way of passing this tax on to anybody. In other words, it is a tax taken right out of the pocket of the broker.

Senator THOMAS. That is one argument in favor of it.

Mr. HINKLEY. Yes, sir; you can not pass it on, and you can not pass it on double. You can not pass it on at all. The tax has to be paid out of the earnings.

Senator JONES. Could you not increase your commissions?

Mr. HINKLEY. Not very well.

Senator JONES. Why?

Mr. HINKLEY. Because they are standard commissions, one-fourth of 1 per cent on the Baltimore Stock Exchange, one-eighth of 1 per cent on the New York Stock Exchange.

Senator JONES. Prices are all rising. Why should not commissions rise?

Mr. HINKLEY. That is a question I can not very well answer. I do not think it could very well be done. Commissions have been fixed for a long time.

Senator TOWNSEND. Do you mean to say commissions have not increased since the war began?

Mr. HINKLEY. No.

Senator SMITH. Percentages of commissions have not increased, but the quantity of business might have increased.

Mr. HINKLEY. No; business has decreased very considerably.

Senator SMITH. I said it might have increased.

Mr. HINKLEY. That is the second point I will come to, and I will bring it up right now; that is, the enormous decrease in the volume of business on the stock exchange. That is attributable to three causes, all of which work together, the decrease of surplus capital available for investment; second, the almost complete absorption of available capital by the United States liberty loans; and third, the greatly restricted output of new issues.

There are very few new securities being floated. Of course, the issue of new securities gives more business to the members of the stock exchange and brokers. So that those two elements together have very materially reduced the volume of the stock brokers' busi-

ness until a great many of them are barely making their office expenses. They are keeping up the organization because they expect the war to be over some day, and, like a great many other lines of business, they keep their offices open in the hope that in the future they will make a profit. But just now a great many of them are doing business at a loss.

Senator JONES. To what extent has the tax which has been placed upon transfers of stock on these exchanges reduced the volume of short sales and speculative sales?

Mr. HINKLEY. I can not answer you that. We have very little of that in Baltimore. Our market is an investment market. There are some people, of course, some brokers, who trade for their own account, and some customers who trade in that way, but our sales are all bona fide sales, whether speculative or not, and are actually paid for in cash and the stock is actually delivered. We have what you might call an investment market in Baltimore, and I think the same applies to other cities which are represented here besides Baltimore.

The Government, as the Senator has suggested, has already imposed that tax on stock transactions, so that we have four taxes now. In addition to the three I have mentioned, we have the tax on the transfer of stock. So that there are four taxes that are imposed on stock exchange transactions, although that particular tax is passed on to the consumer.

Senator THOMAS. You pay State and city taxes also?

Mr. HINKLEY. In New York they have a city tax.

Senator THOMAS. I am speaking about the general State tax.

Mr. HINKLEY. State taxes on transfers?

Senator THOMAS. No; but brokers have some taxable property?

Mr. HINKLEY. Yes.

Senator THOMAS. In addition to these national taxes, you depend upon your business for revenue to pay your State taxes?

Mr. HINKLEY. Yes. I will have to ask one of the other gentlemen of the Baltimore Stock Exchange whether there is a license tax in Maryland?

Mr. H. A. ORRICK. Yes. Of course, we pay a tax on capital, too.

Mr. HINKLEY. There is a license tax in Maryland besides this Government tax. I have emphasized the character of the business of stock brokers, the decline in their business, and, third, the decline in the value of seats on the exchange. The seats on the Baltimore exchange used to be worth about \$6,000. The last sale was for \$4,300, and that sale was not consummated because the purchaser did not qualify. There are three or four seats now offered for sale for \$3,000, with no takers. So the stock brokers are in the position of having seats on the exchange, which, of course, are assets, being cut in half. They are now worth \$3,000 instead of \$6,000. That is another situation that confronts them. They have had that value cut in half.

In addition to that, there is the loss of dues of members in the service. The Baltimore Stock Exchange has only 87 members. In fact, this whole thing involves only a small amount in dollars and cents. I doubt if the whole thing would come to a million dollars, even including the New York Stock Exchange, because I do not suppose there are more than about 2,000 stock brokers, and at \$40 a

piece, that would only be \$400,000, and it might run up a little short of a million dollars. The whole question of this special tax on the business of stock brokers would be a very small amount. Out of 87 members we have six or seven in the service, and we have suspended all their dues. Some members are in the draft, some have died, and it all means a loss of revenue, and their revenues are scarcely sufficient to maintain the business organization.

The CHAIRMAN. Did I understand you to say that out of the 87 members of the Baltimore exchange—

Mr. HINKLEY. Six or seven members are in the service now.

The CHAIRMAN. Military service of the Government?

Mr. HINKLEY. Yes.

Senator SMITH. That is, between 21 and 31. When we go higher up it will get more.

Mr. HINKLEY. Mr. Orrick, can you state how many members of the Baltimore Stock Exchange are now in the service of the Government?

Mr. ORRICK. Seven now in the service.

Mr. HINKLEY. And more that are subject?

Mr. ORRICK. Twenty-eight, I believe.

Mr. HINKLEY. Twenty-eight subject to the draft. The fifth point I make in my brief is that the proposed tax is especially burdensome on members of the smaller exchanges. The value of a seat in New York is \$53,000 and the value of a seat in Baltimore is \$3,000, with no takers, and I have figured in the brief that the cost of doing business in the New York Stock Exchange would come to eight-tenths of 1 per cent of the value of the seat and in Baltimore it is 15 per cent of the value of the seat. That is a little calculation which includes the annual dues of the exchange.

Senator JONES. In other words, you think as to this matter the effect of the tax would be the same as if we applied an equal tax on all automobiles regardless of the size or value?

Mr. HINKLEY. There is a slight rising scale, but it is very slight. Between \$2,000 and \$5,000 it is \$100, and everything above \$5,000 is \$150.

Senator WILLIAMS. The value of a seat on the New York Stock Exchange is \$53,000?

Mr. HINKLEY. About that, I am informed.

Senator SMOOT. Then upon the basis of the cost of the seats in Baltimore and New York, the tax imposed is about in the same proportion as the amounts of money invested. In other words, a man in New York has to invest \$53,000 and a man in Baltimore \$3,000?

Mr. HINKLEY. Yes.

Senator SMOOT. The New York man has 17 times as much investment as the Baltimore man, and therefore the tax should not be the same?

Mr. HINKLEY. But it bears disproportionately on the smaller stock exchange.

Senator SMOOT. I have not figured out exactly what it is. It may be a little different.

Mr. HINKLEY. That calculation shows the cost of doing business on the New York Exchange is eight-tenths of 1 per cent of the value of the seat, and the cost of doing business on the Baltimore Stock Exchange is 15 per cent of the value of the seat.

Senator SMOOT. It is about equal. Eight-tenths of 17 would be nearly 14 cents. So there is only 1 cent difference, based upon the amount of money that you have invested.

Senator GORE. But in Baltimore it is \$100 and in New York it is \$150.

Senator SMOOT. I am speaking of the amount of money it would cost to obtain a seat in New York and the amount in Baltimore.

Senator GORE. The investment.

Senator SMOOT. The investment. It is 15 per cent in Baltimore and eight-tenths of 1 per cent in New York. But in New York it requires 17 times the amount of money to secure the seat, which brings them almost equal.

Mr. HINKLEY. The Senator is entirely correct. The cost of doing business in Baltimore and New York is practically the same, although the value of the seat and the volume of business is very much out of proportion.

Senator THOMAS. This tax is not imposed on the basis of the amount of business you do, but upon the occupation.

Mr. HINKLEY. There are three taxes, one the tax for doing business, which is uniform everywhere. But the other taxes are based on the value of the seats. But it is not on a percentage, but on a sliding scale, which bears disproportionately on the smaller exchanges.

The other point, Mr. Chairman and gentlemen, and one which I can not emphasize too strongly, is the gratuitous service the brokers have given the Government in selling the Liberty Bonds. With the banks and trust companies, they have practically devoted all their time and all the facilities of their offices to floating these loans, making them the tremendous success that they have been.

The CHAIRMAN. In view of the fact that we are all supposed to be doing that—and I hope we all are—if we omit taxes on such grounds we could not get any.

Mr. HINKLEY. We do not ask the committee to omit taxes, but we ask them not to single out stock brokers for a special tax, under the circumstances of the demoralization of their business, and the serious inroads which the war has made on this business. We think under those circumstances this tax, which is trifling in amount, and trifling in the total revenue to the Government, bears very hardly on these gentlemen, with the declining business, and the value of their seats on the exchange cut in half. They are simply living from hand to mouth, almost, until the war is over, when no doubt there will be a revival of stock exchange business, as well as the business in other lines.

Senator JONES. Have you any information as to the profits of a broker on the Baltimore Exchange and the profits of a broker on the New York Exchange?

Mr. HINKLEY. I have not that information. It will be very difficult to arrive at, because you would have to take the average of the profits of a large number of members, and those members on the New York Stock Exchange who speculate of course make losses as well as profits, and some of them at the end of the year will show a loss. But I am speaking of the investment business of the Baltimore Stock Exchange.

Senator THOMAS. I notice on page 140 of this bill there is a tax of \$100 on pawnbrokers. Do you not think that if this bill passes the pawnbrokers are the class of brokers who are going to do the rushing business, in which event we ought to increase that particular item?

Mr. HINKLEY. That is a little outside of the scope of my argument. I do not know whether everybody will be so prosperous, but with the high wages perhaps the pawnbrokers will not have as many calls upon them.

Senator THOMAS. They are doing a pretty good business here.

Mr. HINKLEY. Senator, I thank you very much for your attention, and I will file this brief.

The CHAIRMAN. Please file it with the stenographer.

Mr. HINKLEY. There are three members of the Baltimore Stock Exchange here and two members of the Chicago Stock Exchange, the president and counsel, and perhaps the counsel would like to speak.

The CHAIRMAN. We made this rule when we passed the last revenue bill, and the committee agreed the other day, when we decided on this hearing, to adopt the same rule, to ask the industries appearing to select some one to present their case. We think that two would be quite enough to present the case of any industry. We would not care to hear half a dozen gentlemen, because, necessarily, there would be a great deal of repetition, and the two representatives might state it as well as a half a dozen; in fact, in many instances one might state it just as well. We are proceeding with a little latitude to-day, because we have not quite formulated the line of procedure in all of its details. We are sort of feeling our way. We will hear at least two this morning.

Mr. HINKLEY. There are representatives of the Washington Stock Exchange, the Boston Exchange, and also of the New York Consolidated Exchange present. The New York Consolidated Exchange has a little different matter to present, and that is the payment of the 2 per cent tax on borrowed stock, which bears very heavily, also, on stock brokers on the New York Stock Exchange.

(The following brief was subsequently presented by Mr. Hinkley, and is here printed in full, as follows:)

BRIEF ON BEHALF OF THE BALTIMORE STOCK EXCHANGE IN THE MATTER OF THE PROPOSED TAX UPON STOCKBROKERS.

The Baltimore Stock Exchange most earnestly protests against the proposed tax upon stockbrokers based upon the value of seats on the respective stock exchanges and a percentage of the annual dues paid by members of the exchange, and asks the consideration of the Finance Committee of the United States Senate of the following argument:

I. THE BUSINESS OF A STOCKBROKER IS NOT OF SUCH A CHARACTER AS TO JUSTIFY BEING SINGLED OUT FOR SPECIAL TAXATION AS A BUSINESS.

Stockbrokers carry on a business essential to the economic system, of a character quite analogous to that of the broker who brings together the buyer and seller of produce or other merchandise. These legitimate functions of the broker are governed by rule of the exchange requiring the highest standard of honorable dealing and financial responsibility. The business of the exchange is public, its transactions are recorded, and the strictest rules prohibit fictitious transaction or profiting by the agent at the expense of the principal.

The Baltimore Stock Exchange is particularly an investment market in which the owner of securities which he desires to sell employs the services of a broker at a trifling fixed commission to offer such securities for sale, and parties desiring to purchase securities employ the services of their brokers for a similar commission to effect their purchases.

We can not emphasize too strongly the fact that the business of the Baltimore Exchange is not to any great extent speculative either on the part of the members of the exchange or on the part of their customers. In any case the transactions which take place are small in number and limited in amount, and represent actual cash transactions in which the securities are actually transferred and delivered and the purchase money paid by the broker of the purchaser to the broker of the seller in cash.

II. DECLINE OF VOLUME OF BUSINESS.

The business of the Baltimore Stock Exchange in common with that of all of the smaller exchanges has declined very considerably during the period of the present war. Time has not permitted the compilation of any figures showing the extent of the decline, but it is quite apparent from the most cursory examination of the record of daily sales and is a well-known and self-evident fact. This decline in volume of business may be accounted for by all three of the following factors working together:

1. The decrease of surplus capital available for investment.
2. The almost complete absorption of available capital by United States liberty loan issues.
3. The greatly restricted output of new issues.

We do not hesitate to say that the commissions of the entire membership of the Baltimore Stock Exchange in the past year have diminished as compared with preceding years to a degree that in many cases barely leaves sufficient compensation to pay office expenses.

III. DECLINE OF VALUE OF SEATS ON THE EXCHANGE.

A seat on the stock exchange is an asset of the holder which can be sold in case of his withdrawal from business or in case of his death. Seats on the Baltimore Stock Exchange prior to the entrance of the United States into the war sold for \$6,000. The last sale at the Baltimore Stock Exchange about six months ago was agreed upon at \$4,300, but was canceled because the purchaser did not qualify for membership in the exchange. Several seats on the Baltimore Stock Exchange are now for sale at a price of \$3,000, without finding a purchaser. No seat has been sold for over six months.

In addition therefore to the decline of earnings, each member of the Baltimore Stock Exchange has suffered a loss in his capital account by reduction of the value of his seat from \$6,000 to \$3,000 or less.

IV. LOSS OF DUES OF MEMBERS IN THE SERVICE.

The membership of the Baltimore Stock Exchange is 87. The annual dues paid to the exchange are \$200 from each member. Six or seven members of the exchange are in the service of the United States and their dues have been suspended during the period of the war, and successive Army drafts will undoubtedly take away further members. Several members of the exchange have died during the past year and their seats are for sale. This has caused a very marked decrease of the revenue of the exchange from dues of members and renders difficult the maintenance of the expenses of the exchange from current revenue.

V. THE PROPOSED TAX IS ESPECIALLY BURDENSOME ON MEMBERS OF THE SMALLER EXCHANGES.

The following figures showing the cost of doing business on the New York Stock Exchange and on the Baltimore Stock Exchange are given for comparison:

New York Stock Exchange.

Annual dues	\$150
Proposed 20 per cent Government tax on dues	30
Proposed tax based on value of seat	250
Total yearly charge	430

Estimated value of seat on New York Exchange, \$53,000. Rate of annual charge in proportion to value of seat, eight-tenths of 1 per cent.

BALTIMORE STOCK EXCHANGE.

Annual dues	\$200
Proposed 20 per cent Government tax on dues	40
Proposed tax based on value of seat	200
Total yearly charge	440

Estimated value of seat on Baltimore Exchange, \$3,000. Rate of annual charge in proportion to value of seat, 15 per cent.

VI. GRATUITOUS SERVICES OF BROKERS TO THE GOVERNMENT IN SELLING LIBERTY BONDS.

It is well known that the success of the flotation of the three liberty loans which have been issued has been due in very large measure not only to the active work of the banks and trust companies, but also of the stockbrokers throughout the country. These brokers for a month at a time devoted themselves almost exclusively to the flotation of the loan. Many of them served upon liberty-loan committees, devoting all their time to soliciting subscriptions and speaking at meetings throughout their respective States, furnished the services of their clerical assistants, and undertook the financial obligations incident to the handling of enormous numbers of small subscriptions. Probably no class of professional men have made any greater contribution or greater sacrifice in assisting the Government in the essential work of providing means for carrying on the war. Few classes of the community have exhibited greater patriotism or greater willingness to respond to the call of the Government by not only paying their own taxes and assisting and advising others in the preparation of tax returns, but also in the specific contributions they have so freely made to the common welfare by doing their part in bringing out the universal response to the Government's appeal for funds.

Respectfully submitted.

Counsel for Baltimore Stock Exchange.

The CHAIRMAN. Mr. N. B. Lowes will now be heard.

STATEMENT OF MR. GEORGE N. B. LOWES, REPRESENTING THE CHICAGO STOCK EXCHANGE.

Mr. LOWES. Mr. Chairman, our situation is slightly different from the situation presented by Mr. Hinkley. Our members are members of six or seven other exchanges, or many of them are, and the tax based upon memberships will be a very high tax upon them, and it would seem to us that the tax should be a flat tax based upon the business of the brokers, and not based upon the values of the memberships, because it is necessary, quite often, for brokers to be members of other exchanges in other cities. I would, therefore, suggest that the situation be considered with reference to a tax upon brokers, a flat tax upon brokers, not with reference to the value of their memberships. I believe that is all I care to say.

Senator JONES. What advantages do you get by being a member of several exchanges?

Mr. LOWES. Various connections with firms in other cities that probably would send business, and such things as that. And it is possible there would be some other advantage. I will ask Mr. Thomas, treasurer of the exchange, to answer your question.

Mr. THOMAS. Division of commissions.

Mr. LOWES. Upon business sent from other brokers. I thank you.

The CHAIRMAN. Mr. James Maloney desires now to be heard. Proceed, Mr. Maloney.

**STATEMENT OF MR. JAMES B. MALONEY, REPRESENTING THE
CONSOLIDATED STOCK EXCHANGE OF NEW YORK.**

Mr. MALONEY. Mr. Chairman, yesterday morning we received a telegram that this hearing was to be held here this morning, from the Baltimore Exchange, and I was sent down hurriedly to consult with you this morning to find out what the idea was with reference to a hearing, and we find that the proposition they have presented here we were not considering at all. But we have had under consideration other matters in connection with the brokerage tax which we are going to ask Senator Calder to arrange for a hearing on, if it is possible, representing most likely the New York Stock Exchange, the Boston Stock Exchange, and the Consolidated Stock Exchange, although I myself can only speak for the Consolidated. That was our idea in reference to the tax on loans, return loans, and those things which developed long after the bill went into effect last year. It was not discovered until March that this tax applied on return loans, but that was the interpretation of the Attorney General, and our opinion has always been that the committee never intended, when they enacted the law, to have that tax applied to the return loans. I do not want to take up your time now; but if you can arrange to give us 15 minutes some day and let us file a brief, that will satisfy us.

Senator SMOOT. Do it this afternoon.

Mr. MALONEY. I just came down from Boston.

The CHAIRMAN. You simply want to file a brief?

Mr. MALONEY. And perhaps have some one come and explain a few points.

The CHAIRMAN. How much time would you want?

Mr. MALONEY. Not over 15 minutes.

The CHAIRMAN. We will give you 15 minutes Monday or Tuesday morning.

Mr. MALONEY. It is rather a quick notice, which we received only last night.

The CHAIRMAN. You had better advise the clerk which day you will come.

Mr. MALONEY. I thank you very much. We will do that.

The CHAIRMAN. The next gentleman desiring to present his views is Mr. Cunningham, of New Orleans.

**STATEMENT OF MR. THOMAS F. CUNNINGHAM, REPRESENTING
THE NEW ORLEANS BOARD OF TRADE.**

Mr. CUNNINGHAM. Mr. Chairman and gentlemen of the committee, I just desire briefly to address you covering the brokerage matter. Our situation in New Orleans is somewhat similar to that of the stock-exchange gentlemen who have just addressed you, except that in our case we sell on the floor of our exchange only one class of merchandise; that is, rough rice.

The bill, as we read it, will affect a large number of our members, who do not deal in the particular commodity sold upon the floor, but are brokers of other merchandise, and this tax would apply to them. I allude more particularly to merchandise brokers and manufac-

turers' agents, of which we have a large number, who are members of our exchange. As the tax now stands, what will happen will be that the board of trade will lose a large number of its members, and the revenue will not be forthcoming, but it is not necessary for those brokers to be members of our exchange in order to do business. They are members merely in the voluntary way.

Senator SMOOT. How would they do their business if they were not members of the board?

Mr. CUNNINGHAM. Their business is not transacted upon the board floor. It is transacted from office to office, from store to store, from buyer to buyer. The board furnishes them with quotations and with traffic information, with a number of other things that go to make up the general commerce of the State.

Senator SMOOT. If they were not members of the board, how would they get that information?

Mr. CUNNINGHAM. They would get it from railroad offices, and from various acquaintances, as many brokers do now who are not members.

Senator SMOOT. But not all the information from one source?

Mr. CUNNINGHAM. Not as much; no. But if they have to pay the extra tax, the result is inevitable, those little brokers are small-fry people, and they are going to resign. That leaves our board without its membership, and of course the Government does not get the revenue.

Senator SMOOT. What are the annual dues?

Mr. CUNNINGHAM. The annual dues are \$50. There are a number of similar organizations throughout the South that are somewhat on the same plane. I am not authorized to speak for them, but it just occurred to me that that phase of the situation is being overlooked. It will decimate the membership of a large number of small concerns without bringing in the revenue.

Senator SMITH. This tax would only be a hundred dollars apiece.

Mr. CUNNINGHAM. No; there is an additional tax of \$50.

Senator SMITH. That is on the value of their membership.

Mr. CUNNINGHAM. That is on the value of the seat.

Senator SMITH. You described them as not having seats, and that tax would hardly fall on them.

Mr. CUNNINGHAM. I think their membership would be called a seat.

Senator TOWNSEND. Do you think any tax ought to be imposed on the broker?

Mr. CUNNINGHAM. I do not think any tax ought to be imposed on the broker unless he deals in merchandise as dealt in on the floor of the exchange itself, and then only on the amount of the business he does. We have in our membership at least 75 merchandise brokers. It is not essential, it is not necessary, that they be members of our organization. With the raising of the tax to a hundred dollars, which, of course, they will pay, then comes the additional tax of \$50 to the membership, then come the dues of the organization, and you see it is a pretty stiff tax on the small-fry broker, and the consequence will be that he will resign his membership.

Senator WILLIAMS. And could still carry on his business?

Mr. CUNNINGHAM. Yes, sir.

Senator WILLIAMS. With a little less facility?

Mr. CUNNINGHAM. With a little less facility.

Senator LODGE. You spoke of rice as the principal thing dealt in?

Mr. CUNNINGHAM. Yes; Senator.

Senator LODGE. Do you not also deal in cotton and sugar?

Mr. CUNNINGHAM. Not on this particular board. We have a cotton exchange there. This is a produce exchange, as a matter of fact, although we sell no futures, and the only thing we trade in actively on the floor, where the samples are brought in and put upon the tables, is rough rice. It is sold to the millers, and the millers then complete the finished article and sell it to the jobber and the consumer.

Senator LODGE. But you have cotton and sugar exchanges?

Mr. CUNNINGHAM. Yes; we have two other exchanges, one which sells sugar and the other which sells cotton. We have likewise a stock exchange and a contractors and dealers exchange.

The CHAIRMAN. Did I understand you to say you did not think brokers ought to be taxed at all?

Mr. CUNNINGHAM. No, Senator. I said I did not think they ought to be taxed except upon such articles as were traded in upon the floor of the exchange. In other words, a broker who sells canned goods, under the present bill would be taxed \$50. That is not traded in upon the floor of our exchange. It is not necessary for him to be a member of our exchange at all nor a member of any exchange to sell his canned goods. But if he is member of our exchange he is taxed \$50. If he is not, there is no tax except \$100.

Senator SMOOR. What is the value of your seats?

Mr. CUNNINGHAM. \$50 or \$60, varying with the demand for the stock. It is not a large matter, and yet it is an important matter to the exchanges themselves. They lose heavily in their memberships.

The CHAIRMAN. Have you any further matter?

Mr. CUNNINGHAM. Nothing further, Senator.

The CHAIRMAN. We are much obliged to you. If there is no one else representing any other exchange who wishes to address the committee, we will hear anybody who may desire to be heard upon any other subject. (After a pause.) I assume there is no one here who desires to be heard, and that will end the hearings for to-day.

(Thereupon, at 11.10 o'clock a. m., the committee adjourned until tomorrow, Saturday, September 7, 1918, at 10 o'clock a. m.)

(The following brief and telegram were subsequently submitted by Mr. J. Ralph Pickell, and by order of the chairman are here printed in full, as follows:)

BRIEF SUBMITTED TO THE FINANCE COMMITTEE OF THE UNITED STATES SENATE BY THE COUNCIL OF GRAIN EXCHANGES, RELATIVE TO THE PROVISION IN THE PENDING REVENUE BILL (H. R. 12863) WHICH PROVIDES FOR A TAX ON BROKERS.

The Council of Grain Exchanges is an association composed of the leading commodity exchanges of the United States, and in behalf of the brokers who are members of the exchanges, whom this council represents, we respectfully desire to submit the following facts and suggestions:

Under the provisions of the pending revenue bill brokers are to be taxed \$100, but if they are members of an exchange, such as the Chicago Board of Trade, the leading grain exchange of the world, they are penalized for membership in an organized institution from \$50 up. In the case of the Minneapolis Chamber of Commerce, under the provisions of this bill, a broker would have to pay about \$250. Under the rules promulgated by the Food Administration, any-

one not a member of an organized exchange may bid for wheat, controlled in price and distribution by the United States Government and deliver said wheat to the United States Food Administration, receiving therefor the same compensation that the broker of an organized exchange may receive under the rules of the Food Administration, and yet under the provisions of the revenue bill such a broker, uncontrolled by the rules of any organized exchange, would not be required to pay any tax. Obviously this is a discrimination and it is the purpose of this brief merely to point out the discrimination and then to rely upon the wisdom and statesmanship of the Members of Congress to remove said discrimination, which is unfair and which will tend to discourage organized and properly controlled business.

The brokers, members of grain exchanges, are desirous of doing their full share to win the war. If it be necessary that they should be taxed \$100 and then more in order that the war may be successfully financed they will not complain, but they do believe it just that if their memberships in organized exchanges are to be taxed that those who accept opportunities to transact the same kind of business outside of exchanges should be taxed a like sum or else the tax on the brokers' memberships in exchanges should be abolished. Brokers conduct their business under the very careful scrutiny of the officers and directors of the exchanges with which they are affiliated. The rules governing them in the handling and distribution of the cereal crops are solely for the protection of the public and carry severe penalties for any violation thereof.

The following rules are taken from those of the Board of Trade of the city of Chicago and are self-explanatory:

"Sec. 11. No member of this association is allowed under any circumstances to be both principal and agent in any transaction in any of the commodities dealt in under the rules of this board. Furthermore, no member of this association in any transaction in any of the commodities dealt in under the rules of this board shall allow himself, directly or indirectly, either by his own act or by the act of an employee or of a broker or other member of the association, to be placed in the position of agent for both seller and buyer.

"Sec. 31. When any member of this association, knowing himself, or the firm in which he is a partner, or the corporation of which he is an executive officer, to be in an insolvent condition, shall make any contract on his own account, or on account of such firm or corporation, under the rules of this association, whereby pecuniary loss shall result to any other member, or to any firm or corporation entitled to transact business on this exchange, he shall be suspended or expelled at the discretion of the board of directors; or, when any member of this association, knowing himself, or the firm in which he is a partner, or the corporation of which he is an executive officer, to be in an insolvent condition, shall accept on his own account, or on account of any such firm or corporation, any money or security or securities as margins from any customer on any trade or trades made under the rules of this board, whereby pecuniary loss shall result to the person, firm, or corporation depositing such margins, such member shall be suspended or expelled at the discretion of the board of directors."

These rules insure fair treatment of the producers and consumers that could not prevail except through a duly organized exchange. The exchanges also insure the handling of the cereal crops economically and efficiently, and that this is recognized by the Government is evidenced by correspondence with the United States Food Administration.

One letter to which we refer, under date of September 3, says, "We appreciate fully the importance of the grain trade, and know of no industry more essential."

A statistical division of the United States Food Administration also recognizes the value of organized exchanges, and says, under date of August 29, "I wish to thank you very much for your trouble in supplying us with this information and assure you that it will be of much use to us."

Also, a letter from the United States Civil Service Commission of August 22, expressing its appreciation of our interest and offer of cooperation.

Also, under date of August 30, from the National War Service Committee, saying that "It is such patriotic cooperation that you gave us that made our drive the success it was."

Also, from the Bureau of Markets, Mr. Chas. J. Brand, Chief, under date of July 17. "The bureau greatly appreciates the manner in which the officers and members of the Board of Trade have cooperated in this investigation and the readiness with which they have opened their books and offered assistance."

These are only a few of the many letters that we desire to call to your attention to emphasize the fact that the organized exchanges are of great value to the Government and to the producers and consumers; whereas, the class of brokers not controlled by rules or regulations of an exchange and under no restrictions in their relation to the public would be more susceptible to personal gain, and could be of practically no help to the Government. Therefore, to discriminate in favor of such brokers to the extent of from \$50 to \$250 per annum puts a penalty where it does not belong, and this could not have been the intention of the framers of the law, except through a lack of information relative to the business of the grain exchanges conducted, as they are now, in strict cooperation with the United States Food Administration.

A recent member of a board of investigators, appointed by the Bureau of Markets to examine into our affairs, reported, in substance, as follows:

"That the board of trade is an efficient market organization, operated at low marginal cost under democratic form of self-government by the board of directors in the public interest."

Shall the members of such organizations be penalized in favor of competitors who are under no exchange control?

J. RALPH PICKELL,
Secretary, 417 Postal Telegraph Building, Chicago, Ill.

ST. LOUIS, MO., September 18, 1918.

Mr. J. RALPH PICKELL,
Congress Hall Hotel, Washington, D. C.:

In behalf of the members of the St. Louis Merchants' Exchange I would appreciate your making a vigorous protest against that feature of the revenue measure which contemplates an arbitrary tax on brokers doing business on grain exchanges. It savors of class legislation, and is manifestly discriminatory and unjust. Most of the brokers are performing a patriotic work in materially aiding in the distribution of the cereal crops of the country; others represent only flour and feed mills and can only conduct their business to advantage on exchanges.

JOHN O. BALLARD.

DULUTH, MINN., September 18, 1918.

J. RALPH PICKELL,
Congress Hall, Washington, D. C.:

Members of the Duluth Board of Trade wish to file a protest against brokerage tax, feeling same to be unjust and uncalled for. We appreciate your kindness in presenting protest in our behalf.

DULUTH BOARD OF TRADE,
By M. L. JENKS.

OMAHA, NEBR., September 18, 1918.

J. RALPH PICKELL,
Congress Hall Hotel, Washington, D. C.:

You are hereby authorized to represent the Omaha Grain Exchange and file protest on our behalf against brokers' tax provided for in revenue bill.

F. P. MANCHESTER, *Secretary.*

BUFFALO, N. Y., September 18, 1918.

J. RALPH PICKELL,
Secretary, Congress Hall Hotel, Washington, D. C.:

Thanks for your telegram. The interests of all grain exchanges are identical as regards brokers' tax, and this is your authority to enter protest for corn exchange along the same lines as Chicago Board of Trade protest.

D. M. LEWIS,
President Corn Exchange at Buffalo.

KANSAS CITY, Mo., September 19, 1918.

J. RALPH PICKELL,
*Secretary Council of Grain Exchanges,
Congress Hotel, Washington, D. C.*

Please file following protest with Senate Finance Committee:

On page 139, new revenue bill, there is a provision requiring all brokers to pay an annual tax of \$100. This includes every person whose business it is to negotiate purchases or sales of produce, but where these brokers are members of an exchange there is an additional penalty of \$50 to \$150, depending on the value of the exchange memberships. This is a serious discrimination against members of an exchange, due probably to lack of information regarding difference in standing between produce brokers who are members of legitimate exchanges and those who have no connection with any business organization. Members of all exchanges are, in conducting their business, subject to careful scrutiny by officers and directors and there are very strict rules covering all such transactions designed to protect both buyer and seller in making trades through any broker who is a member of such exchange, and there are very heavy penalties imposed for violations of any of these rules. Our rules governing exchange transactions insure proper treatment of all parties interested, which would not be possible except for our organization. We desire to impress upon you the fact that, aside from the protection offered people buying and selling in our exchange, the complete organization of the grain business insures the handling of the crops on the most efficient and economical basis, all of which has been fully recognized by the Government through the United States Food Administration, and it does not seem just that members of an organization should be penalized while other dealers acting entirely independently without the supervision of an efficient body should be favored by a much lower tax.

O. A. SEVERANCE,
President Kansas City Board of Trade.

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TO PROVIDE REVENUE FOR WAR PURPOSES.

SATURDAY, SEPTEMBER 7, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 o'clock a. m., in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present: Senators Simmons (chairman), Smith, Thomas, Jones, Gerry, Nugent, Lodge, McCumber, Smoot, Townsend, and Dillingham.

The committee resumed the consideration of the bill (H. R. 12863) "to provide revenue, and for other purposes."

The CHAIRMAN. Gentlemen, we will proceed now. Mr. Marsh, we will hear you first this morning. Before you begin I want to make this statement: Yesterday a question was asked here as to the construction placed by the committee on the House bill. I stated then that the persons appearing to discuss the bill would have to make their own construction. I want to say now that the committee is considering this bill extrajurisdictionally, so to speak; that is, we are discussing it extrajurisdictionally while the House is considering it. Under those circumstances the members of the committee sitting as a committee feel a delicacy in expressing any opinion about the bill or its meaning, because we do not wish to do anything that might have the appearance of attempting to influence the action of the House while it is considering the bill. I want to make that statement, not especially for your benefit, Mr. Marsh, but as a general statement. You may proceed now.

STATEMENT OF MR. BENJAMIN C. MARSH, EXECUTIVE SECRETARY, FARMERS' NATIONAL COMMITTEE ON WAR FINANCE.

Mr. MARSH. Mr. Chairman and gentlemen, I am the executive secretary of and appear on behalf of the Farmers' National Committee on War Finance. I may state, by way of introduction, that this committee was organized some time ago by representatives of large farming organizations, State granges, farmers' unions, the Gleaners, the American National Live-Stock Association, and the American Society of Equity. It was organized about a year and a half ago, and reorganized some months ago, to meet the present situation.

The CHAIRMAN. You are representing the Farmers' National Committee on War Finance?

Mr. MARSH. Yes, sir.

The CHAIRMAN. Are you the only gentleman who wishes to speak?

Mr. MARSH. There will be other men here later, I hope. The date of the hearing has been changed a little and I am not sure whether the other gentlemen will be here or not.

The CHAIRMAN. As Senator Lodge suggests, we can not hear the statements of several representatives of the same industry; it would take too long. Do you expect others to appear later?

Mr. MARSH. There will be probably only one other.

The CHAIRMAN. Then we can give you 20 minutes. Will that be sufficient for your purpose?

Mr. MARSH. Of course, I can tell better whether it will be sufficient after I have seen the result of my remarks on the committee. If that is what you assign, I will take it with pleasure.

The CHAIRMAN. Well, take 25 minutes, and we will hear one other representative.

Mr. MARSH. I thank you very much. We will try to make arrangements with the clerk for the appearance of the other gentleman later.

May I call your attention to the copies of the Farmers' Open Forum which have been distributed here and which contain an article entitled "Credit monopoly and the revenue bill," by Gov. Arthur Capper, who is chairman of the Farmers' National Committee on War Finance.

Now, the farmers of the country stand foursquare back of President Wilson's statements: "Every power and resource we possess, whether of men, of money, or of materials," is to be devoted to winning the war. "It is our duty, I most respectfully urge, to protect our people, so far as we may, against the very serious hardships and evils which would be likely to arise out of the inflation which would be produced by vast loans." "We shall naturally turn, therefore, to war profits and incomes and luxuries for the additional taxes."

Now, of course, the farmers of the country do not feel under the same restraint in criticizing the pending revenue bill introduced by the Ways and Means Committee as the chairman has indicated that this committee does at this time. The farmers are keenly disappointed in that revenue bill. It should raise at least four billion dollars more than it does raise. I quote from a resolution of the American Federation of Labor, although I am not speaking officially for them in any way, but it is striking that the farmers and labor forces of the country are a unit in holding that the major part—many of them think all—the costs of the war should be raised by current taxation. The resolution of the American Federation of Labor, which was passed at its annual meeting in St. Paul, reads as follows:

Resolved, That the American Federation of Labor urges Congress to levy taxes on war profits, swollen incomes, and on land values, to an extent that during the period of the war will provide by taxation at least 50 per cent of the expenditures of the Government in any one year.

The CHAIRMAN. Pardon me; when you say the expenditures of the Government do you mean 50 per cent of the amount this Government expends, or 50 per cent of the amount it spends and in addition thereto 50 per cent of the amount it loans to the allies?

Mr. MARSH. I can not speak officially for them on that point. I think they mean 50 per cent of the whole cost of the war.

Senator SMOOT. That is not the cost of the war.

Mr. MARSH. Well, now you raise a point which I did not want to go into, but I shall be glad to do so, and here I can not speak officially for the farmers. Many of them express the belief that some of the allies may not be able to pay their loans, and at the conclusion of the war we may want to pay them ourselves as a gift to the allies. I think it is safe to write down the loans as a cost of the war. None of us would want to fight the allies to compel them to pay the loans we have advanced.

Senator SMITH. The bulk of the loans will certainly come back without any war.

Mr. MARSH. Yes; but we may want to give it to them.

Senator SMITH. That is absurd. I think the idea of our giving Great Britain the money we loan to her is a proposition that the British Government would really consider an insult.

Mr. MARSH. How about Belgium and Russia?

Senator SMITH. That is very much similar.

Mr. MARSH. How about France?

Senator SMITH. Well, France can take care of herself. The French are the most resourceful people in the world.

Mr. MARSH. All right; I do not enter into a discussion of that; but I suggest this, then, as the farmers' position: We ought to pay all we can of the cost of the war as we go along, at least 50 per cent or 60 per cent or 80 per cent. We ought not to pile up enormous debts. I am sure you gentlemen will all take time to read this article by Gov. Capper, but may I just quote a little section which bears directly on our position?

Senator JONES. I would like to interpolate that a resolution was introduced in the Senate some time ago by the Senator from Iowa, Mr. Kenyon, donating to France all the money which we have advanced to that country.

Senator SMOOT. Congress will have something to say about that and France will also.

Senator SMITH. It has not passed?

Senator JONES. No; it has not passed.

Mr. MARSH. Let me interpolate this question: Would it not be a tremendous encouragement to the French soldiers and the people who have made these great sacrifices if there were an indication that America would not mind doing it? Here is what Gov. Capper says:

Selfish financial interests ignore the fact that the settlement of national debts after this war presents a problem more difficult than beating the Kaiser. This latter is assured. We are going to do it. And the national debt is a dead weight on a nation's progress and will rest in chief measure upon the farmers of the country who must pay the larger part of it. This is clearly the intention of the undemocratic selfish financial group of this country which seek to-day as ever to dominate not only the domestic but the foreign policy of the United States.

The farmers hold that no patriot will ask for an income of over \$100,000 during the year and that no one but a patriot should be considered during the war. A very important member of the Ways and Means Committee said to me, "You can not leave any man with an income of over \$100,000 during this war. You have to take it either in taxes or in loans." Therefore it resolves itself into this question—and this is where the battle of democracy is being fought

out in America, by reasoning and by argument, as it has to be fought out by physical force in France and elsewhere—Are you going to leave John D. Rockefeller and the other people with big incomes a lot of their income and borrow it from them at 4 or 4½ per cent or are you going to take everything over \$100,000 in taxes?

I have been advised that what I might say might be construed as a criticism of the impending fourth liberty loan. It is not a criticism in the slightest degree. We are now discussing the ratio between bonds and loans. The farmers will not, I think I can say, readily forgive Congress if they do not pass this revenue bill before they call for another liberty loan, for we want to see what sincerity there is in the statement that we are going to devote all our resources to the winning of the war. There is not a farmer or laboring man earning fair wages who ought not to contribute heavily toward the liberty loan. I want to see the working people loan to the Government and men of enormous wealth taxed. I want to see the rich people put their money into the war, not as a loan but through taxation. The question is not, however, how much you or I give; it is how much we have left. Now, I take these rates of income taxes. From an income on \$5,000,000 it is proposed to take \$3,527,000, leaving that individual very nearly a million and a half income during the war.

Senator SMOOT. If we take 80 per cent by our war profits, there will not be very much left.

Mr. MARSH. This has nothing to do with the war-profits tax.

Senator SMOOT. That is why I speak of it.

Senator LODGE. That is where the income comes from.

Mr. MARSH. After a man has paid his war-profits tax, whether it is 80 per cent or 90 per cent, he is then taxed on his net income. We want 90 per cent of the war profits. We do not want to penalize anybody, but we let slip about a couple of billion dollars in war profits last year. It has somewhere gone into recouping the people who built the plants. When a man constructs a plant the productiveness of which ceases after the termination of the war there is no intention of asking that he be taxed so that he will lose after the war, but we have had two or three years to get in shape and want to point out how you can raise easily \$12,000,000,000 or \$12,500,000,000 by taxation for the present fiscal year, and we urge very strongly that you will do it.

The war profits subject to taxation during this year are estimated to be approximately \$4,305,000,000. May I add that we would be glad to submit to the committee later a copy of a long report submitted to the Ways and Means Committee on this point of war finance, which you may like to look over. Some officials in the Treasury Department were good enough to give me some estimates. The war profits subject to taxation during the present year are \$4,305,000,000. A tax of 90 per cent on these profits will yield \$3,875,000,000, or \$675,000,000 more than the House bill estimates. At least \$6,000,000,000 can be raised by the direct income tax, or \$4,582,000,000 more than the House bill estimates.

In 1918 it is estimated that approximately \$14,000,000,000 will be received by people making income-tax returns, from which \$3,500,000,000 should be deducted as dividends. This averages about \$4,600 per family.

We propose taking all incomes over \$50,000. They have figured it out that most folks can get along on \$50,000 a year during the war. They can cut down all around. No one has a right to start any industry during the war that is not approved by the Government. We ought to stop a lot of these nonessential industries. We ought not to let people consume luxuries.

Senator SMITH. What do you mean by their not having the right to do it? They can do so if they want to.

Mr. MARSH. I mean to say that the sanctions of patriotism ought to prevent their doing so, and if the sanctions of patriotism do not prevent them they should be treated just exactly as the I. W. W. were treated.

Senator SMITH. You mean that it would not be right for them to do so.

Mr. MARSH. It would not be right for them to do so, and I think the Government should say they can not.

The CHAIRMAN. You mean that the Rules Committee would not give its approval?

Mr. MARSH. Certainly, and they ought not to be allowed to go out in the market and compete for capital. We are out to win this war and not to enable a few people to get rich during the war. It is perfectly legitimate to take in taxes at least all of a man's income over \$100,000.

Senator LODGE. How much would it yield if that were done?

Mr. MARSH. Just taking that would not yield very much.

Senator LODGE. How much would it yield in taxes if you did it?

Mr. MARSH. I can not give you the exact figures.

Senator LODGE. That is rather important in making up a tax bill.

Mr. MARSH. I have the figures in my brief in black and white.

Senator LODGE. Are they Treasury Department figures?

Mr. MARSH. They are Treasury Department figures so far as the amounts are concerned, taking, of course, the average, because, unfortunately, they do not have publicity as to incomes over \$25,000 or \$50,000. I think you also ought to go further down. I am going to say to you gentlemen exactly what I said to the Ways and Means Committee, and I am speaking for the farmers. My wife and I both work and work very hard. There is no eight-hour day for us. We will have a joint income this year of about \$4,300. I said to the committee: "I want to pay \$300 or \$400 in taxes this year. I can not look the soldier boys in the face if I do not." I have been talking to the soldiers at Camp Meade on the economic issues we have here, and I am going to talk to others. I can not look those men in the eyes—I have a lot of dependents, too—if we stay over here and object to paying \$300, or \$400, or \$500 tax, my wife and I together, out of our income. I put it up to a lot of farmers from as far west as the Pacific coast recently in half a dozen big farming States. I said, "What do you men think about this?" They said, "If Congress should take all incomes over \$100,000 we would not object." Simply taking all over \$100,000 would not raise over a few hundred millions extra.

I have suggested here rates on incomes down to \$3,000 or \$4,000; 10 per cent on the net income of those receiving from \$3,000 to \$4000; 20 per cent on the net incomes of those receiving from \$5,000 to

\$10,000; 35 per cent on the net incomes of those receiving from \$10,000 to \$20,000, and so forth. I do not try to exclude anybody. We have to admit the fact that there is a tendency during this period of large wages on the part of some working people to spend luxuriously, and furiously, I was going to say; and the knowledge that they will have to pay heavy taxes would be a great help to economy. As Gov. Capper points out, if we know we have to pay a tax, we are going to save money. Now, we have to save money, but it is perfectly ridiculous, gentlemen, to say, is it not, that with a national income estimated very conservatively during this year at \$72,000,000,000—and I take the figures of men like Prof. B. M. Anderson, jr.—

The CHAIRMAN. Do you mean the net income?

Mr. MARSH. No; a gross national income received of \$72,000,000,000.

The CHAIRMAN. That does not help us much. What we want to know is the net income. Gross income might not take two-thirds of it, and there would have to be deductions before you would get to the net.

Mr. MARSH. I think not in the way I use the word "gross." I mean to say, with the income received from dividends, from wages, the income which we have to live upon; not gross. I mean to say the total. Your point was quite correct, and I thank you. I should have said the total. The total national income is estimated at about \$72,000,000,000. We can surely raise one-sixth of that by taxation, and I hope we will not rely to any such extent as Mr. Kitchin suggested yesterday on a \$16,000,000,000 bond issue. Gentlemen, we have no right to saddle a profiteer upon the neck of every soldier who comes back from the war, and that is what is contemplated by the pending revenue bill. You know and I know that if this war lasts three years—two years more—

The CHAIRMAN. You say, you know and we know. We do not know that.

Mr. MARSH. I say, if it lasts two or three years more it is going to cost us \$75,000,000,000 to \$100,000,000,000. Then, demobilization may cost \$10,000,000,000 or \$15,000,000,000. We are up against an enormous expenditure. It is true that we have the lowest national debt in proportion to national wealth of any of the countries at war. The figures Gov. Capper quotes here, but they have been rising very rapidly ever since he wrote this article two or three weeks ago. Our ratio is changing very remarkably. And the farmers know that a big national debt is an awful burden on the industry of the country.

We do not object to taxes on luxuries, but we suggest that you have overlooked one thing, one class of property almost absolutely exempt, and that is the value of lands held idle, or practically idle, for speculative purposes. A large number of farmers will pay an income tax with a \$2,000 exemption. They will pay an income tax, and they are glad to do it; but they think that you should raise at least \$500,000,000—half a billion—by taxing the value of unused and inadequately used land held for speculation, together with these other taxes.

Senator SMITH. You would treat it all as held for speculation, would you, if it were unused and unprofitable?

Mr. MARSH. I think so because it is increasing in value very rapidly. For instance, the land in New York City is worth as much as land in 20 agricultural States of the Union; and rents are going up tremendously in New York City. That is my voting residence. I have been there for 11 years and I know the situation pretty well. You gentlemen may know that the land in every American city and farm land every where is largely monopolized in a few hands. We should take 80 to 90 percent of war profits and all incomes from over \$50,000 to \$100,000. But, as I am informed by officials here, many people to escape taxation for this war are putting their money in vacant land and being advised to do so by lawyers. There is no income from vacant land. It lies still and increases in value.

Now, you will notice, gentlemen, that our proposal will make it unnecessary for you to adopt the position of those who hold that booze will win the war. There are such people. There are people who hold that booze will win the war by creating a billion dollars in revenue and increasing the efficiency and happiness of workers. Of course, there is that point of view, but you will notice that the British labor party are unequivocally out for war-time prohibition. I am not arguing that, but we do point out to you the fact that if you will adopt the system of taxation which we suggest, it will not be necessary to have recourse to that position, and add booze to the factors which are going to win the war. You will not have to rely upon that for revenue and efficiency, certainly not for revenue.

We ask that you take into consideration the position and attitude of the men who are actually doing the fighting. Gentlemen, the Ways and Means Committee has been several months figuring out how to be tender with the dollars of America, and in less than two weeks you enacted the necessary and commendable bill to provide the adequate man power. What impression does that produce upon the average soldier or sailor? With the President coming up and asking Congress to pass this revenue bill promptly you leave, under the terms of this bill, some men in America incomes of \$3,000,000 or \$4,000,000 from utterly unearned sources, and one \$20,000,000 from the monopoly of oil-pipe lines, and so forth.

Senator JONES. If it will not interrupt you, let me ask you a question to get your idea as to how we would tax this unused land. How would you do that?

Mr. MARSH. I will answer briefly, if I may, and then submit a bill later that has been prepared covering this matter. In most States there is now a classification of assessed property. This bill provides that the value of all lands shall be obtained, the existing records being used where necessary.

Senator JONES. If I understand you, your argument is based on this idea that there is an unearned increment there, that the lands are increasing in value, and that that increased value is actually income, and it is that which you seek to reach. Am I correct?

Mr. MARSH. The increase in value of land is not in the hands of the individual, necessarily, unless he attempts to sell it or rent, and then if you have ever bought land you know that it is a very actual fact, that increase in the value of land. It is not debatable, is it? The value of land is increasing constantly.

Senator LODGE. All land?

Mr. MARSH. No; but land in the aggregate.

Senator SMOOT. Lots of it is decreasing.

Senator McCUMBER. Two-thirds of the land in the city of Washington has not increased in value in 15 years.

Mr. MARSH. Then, why did you not pass the antirent profiteering bill? Do you mean to tell me that rents here have not increased?

Senator McCUMBER. We have passed one.

Senator SMITH. We have passed two. Are you living here?

Mr. MARSH. Yes; I had to come down and bring my family here. I am working at the Washington headquarters of the Farmers' National Committee on War Finance. I would like to refer you to the report made by the late Congressman Henry George on land values in Washington. I would be glad to get it and send it to you. Land values are increasing.

Senator McCUMBER. Increasing in some sections and decreasing in others.

Mr. MARSH. Granted; but whether it increases or decreases is not due to the ingenuity or work of the individual who chances to hold title thereto, but exclusively to the industry and presence of population.

Senator SMITH. The world's population is increasing and the land is not. Therefore the land must increase in value.

Mr. MARSH. That is inevitable. I do not need to debate an axiom. I did not mean to get off on the land question because, frankly, that is not the only important item in the program of the farmer. It is only one of the items by which this revenue could be raised. Some of the farmers from out West told me—and I have talked with many of their representatives within the last 10 days—"Here is the situation we are up against. The boys have been taken from the farms. They have volunteered and went gladly. They sold their equipment at a loss. Unfortunately, some folks would not pay them full value. They went into the Army, and they are coming back by the millions in a few years. They have not saved much of their \$30 a month, we will concede. What are we going to do with them?"

I talked last night with a man just over from England, a very well-known business man. He told me what the British boys in the trenches were saying there. And, by the way, may I interject the statement that our boys who are coming back own no land here. The English boys call England "Blighty." This man told me that the boys in the British Army were saying, "We are fighting for Old Blighty. We do not own a square inch of Old Blighty, but you can be jolly sure that when we get back we are going to have a bit of Old Blighty that we are fighting to save." And they are going to get it and our boys are going to get it.

Land values are going to be tremendously inflated in some sections; not in all sections. When these boys come back by the millions, some of them cripples, some of them armless, some of them legless—we hope not very many—what are we going to do with them, gentlemen? The after-the-war problem is more serious than the present war problem, since we have unity of command. If you tax land values, you are going to make it easier for those boys to be settled on the land. I have talked with some of the gentlemen of the Senate about these after-the-war problems, and they are very serious. If I should tell you some of the things the boys in

khaki have told me you would think I am pretty radical. I am not. I have talked straight to them and they have talked straight to me, and while I have addressed audiences in Carnegie Hall and Madison Square Garden, I have never had such frank and sincere approval of just the point I am presenting to you here on behalf of the farmers as I have received from the big crowds of boys in khaki, most of whom have now gone to France.

Now, I have taken the time you have assigned me. Those are our suggestions. We do not see any need for all these detailed taxes on consumption and things of that sort. I hope you will not proceed to rob the workingman by consumption taxes, because that is all consumption taxes are, indirect robbery of the workers. I think it would be better for the average workingman and farmer if you would reduce the exemption a little, if necessary, rather than impose any consumption tax. It would be easier for the farmer in the long run. Those four taxes I mentioned will raise all the revenue you need to finance the war, and a direct income tax is an honest tax, because you know what it is.

Now, I criticise, on behalf of the farmers, the suggestion of the Ways and Means Committee and the Treasury Department about these consumption taxes on luxuries.

Senator SMOOT. What is your business?

Mr. MARSH. I am now secretary and director of publicity of the Farmers' National Headquarters. I am executive secretary of the Farmers' National Committee on War Finance. I am secretary of the Farmers' National Committee on Packing Plants and Allied Industries, a committee organized to carry into effect the essential recommendations of the Federal Trade Commission. I am assistant secretary of the Farmers' National Wheat Growers' Association.

Senator SMOOT. You are not a farmer, then?

Mr. MARSH. No; I am not a farmer.

Senator SMOOT. Do you live in New York?

Mr. MARSH. I have lived in New York, but I have worked on a farm. I worked a good bit of my way through college, getting up at half past 4 in the morning and working until late at night.

The CHAIRMAN. Mr. Marsh, you have been interrupted a good deal. Would you like to have more time?

Mr. MARSH. I would like to have two or three minutes more in which to finish. Occasionally, of course, you gentlemen have asked me questions, and in answering them I could not speak officially for the farmers.

Senator JONES. Let me see if I do not get your point of view. You consider that all taxes, however levied, must come out of incomes?

Mr. MARSH. Out of production.

Senator JONES. It is a question of whether you should get that income directly through an income tax or indirectly through a consumption tax, and you favor getting it all by direct taxation?

Mr. MARSH. I always favor direct taxation, because then you know just what is happening. When you have indirect taxes the man who advances the tax will add his profit and his commission on that tax, and the purchaser of the product pays more.

Senator SMOOT. But you are always perfectly willing to have exemption on the direct taxation?

Mr. MARSH. The poorest man in America pays to-day infinitely more taxes proportionately than the richest man. Will you tell me what I can eat or wear that I do not pay a-tax on?

Senator SMOOT. I have not the time to tell you, but I could give you a list as long as your arm.

Mr. MARSH. I can prove every statement that I make, Senator, to the satisfaction of every workingman and every farmer in America.

Senator SMOOT. Of course I know you can.

Mr. MARSH. I think they have given the verdict in the last two Presidential elections on that point. I do not mean to discuss politics but economics, and they ought to be the same thing. The farmers ask that you save us, so far as possible, from a big war debt. The farmers have been accused of disloyalty. I know practically no cases where the court has sustained the charges. And the farmers have been the leaders in the liberty loan campaigns.

The CHAIRMAN. They have not as a class been accused of disloyalty.

Senator SMOOT. That is the first I have heard of it.

Mr. MARSH. I will send you some documents in which that statement is made.

Senator SMOOT. By some wild-brained fellow that is speaking for himself and nobody else, but the American people do not believe it.

Mr. MARSH. May I send you some copies of the Congressional Record of the Senate?

Senator TOWNSEND. You can prove anything by that.

The CHAIRMAN. I think, Mr. Marsh, it would hardly be fair to let it go out that farmers as a class are regarded by any responsible persons as being disloyal. Certainly there is no more loyal or patriotic class of our citizenship than the farmers, and I will add the laboring man, too.

Mr. MARSH. Yes; I think their interests are identical, thank God. They are learning that fact, which means the end of privilege and monopoly.

The CHAIRMAN. If you will permit me to say so, I think all our people are patriotic. There may be some that are not, but considered in the aggregate our people are intensely patriotic.

Mr. MARSH. I agree with you, and it is only very small: but, my conscience, what a splendidly vocal crowd the unpatriotic one is, and it is efficient. But the farmers are not justly accused of being unpatriotic, nor will they be accused of being unpatriotic in telling you that they want this distinction between the treatment of boys and property stopped, and that the present proposed revenue bill is unjust in not providing that \$12,000,000,000 to \$13,000,000,000 should be raised by taxation.

We can win this war in a way which means peace and prosperity for this country, or we can win this war against kaiserism in Germany in a way which means a revolution in this country after the war. We have to face that fact. And the farmers maintain that we have to put the interest of the property and the men of this country on an absolute parity. To do that you can not permit any such revenue bill to be enacted as has been sent over by Mr. Kitchin and his conferees, who have done good work, but I have talked to them just exactly as I have to you, both publicly and privately. You can not do it, gentlemen.

I would like to make some statements here that were made to me recently, but I am afraid it would be indecorous, as to why the income-tax rates are not higher. But I would submit to you that any man in the United States who intimates that he is not going to support the war, or will interfere with it, if the Government takes all his income over \$50,000 or \$100,000 while protecting him in his business through the War Finance Corporation—any man who intimates that—and some of them have—should be given the same treatment as the I. W. W. in Chicago were given a few days ago. There is lots of room yet in the Federal penitentiaries for rich men who do not want to make the same proportionate financial sacrifices as the poorest people of the country.

This is really a test, gentlemen, this revenue bill, and it is so regarded. I happen to know most of the farm leaders and labor leaders of the United States. I have talked with them and I know how they feel about this proposition. I will get out and work for the liberty loan, tooth and nail, but I prefer, gentlemen, to pay my share in taxes. And most of them do, too, and apply the same principle, because, just think, here is what you do: Here is a man with an income of \$5,000. What does he pay? One hundred and eighty dollars. That is all proposed under this bill. Gentlemen, we submit that \$300 or \$400 or \$500 is the very least that a man with an income of \$5,000 should want to pay and ought to pay.

The size of this next liberty loan will be vitally and directly affected by this revenue bill. Let me repeat that the farmers see no reason why you should not pass this revenue bill within two weeks, the same time in which you passed that necessary man-power registration act. In other words, we have got to realize that the American people are following the President in the purposes for which he declares we entered the war, which mean an entire change in our economic and industrial system, and they want to see that change started during the war in order that they may be completely assured, incontrovertably assured, that we are really going to win the war in America that we win in Europe. You know there is such a thing as the possibility that we could lose in America the war that we win in Europe. But this revenue bill is a test of the sincerity of both the Republican and Democratic Parties.

Senator JONES. Why do you propose to raise only 50 per cent by taxation? Why not raise it all by taxation?

Mr. MARSH. I think I corrected the impression which I seem to have given. I did not stipulate what percentage. I said at least 50 per cent. Personally, as I said to the Ways and Means Committee, there is no more reason why you should say "We should raise 50 or 40 or 33½ per cent or 90 per cent" than why you should say "We will send 1,000,000 men to France and no more." I do not think you ought to put a limit on it.

Senator JONES. Then, why let one man have \$50,000 income and another man only \$2,000 or \$3,000 or \$5,000?

Mr. MARSH. Simply for the reason that you have to temper the wind to the shorn lambs of privilege in this country. That is the only logical reason.

Senator SMOOT. And, of course, to do justice, we ought to take it all away from them and make them all equal. That is the idea?

Mr. MARSH. Since we have been doing that a little bit with the fellow with an income of \$2,000, I do not think it would be bad to do it with the fellows with over \$50,000, and while you have to be practical to do otherwise than I suggest, you have to say that the organized farmers and laborers are a bunch of idiots. They know the fight that is on in this country and throughout the world. They understand what this is all about, and they propose to see that the thing is put through in this country and that nobody makes a dollar unjustly out of the war.

Now, we are a rich country. We have got to get revenue out of incomes; out of production primarily; production, and more production. I think we all agree to that. Mr. William Kent brought that out very clearly in his address to the Ways and Means Committee. We have to increase production. Now, a tax on unused land values will help that. But, gentlemen, a debt of seventy-five or even fifty billion dollars on the industry of this country after the war is going to be a very serious thing. According to the press—I have not seen the Congressional Record yet of this morning—Mr. Kitchin said yesterday that we could never look forward to a smaller national budget than \$4,000,000,000. That is one-third more than the total expense for all governmental expenses, National, State, and local in 1915, before we entered the war.

Now, forty or fifty billion will be the lowest debt at the rate we are going now, if the war goes on for two years longer. It will be easier and better for every legitimate business interest, we submit, farming included, and workingmen included—they are all in industry—if we pay two-thirds or 60 per cent of the cost of the war by current taxes. It will come pretty hard, but I have read a good deal about these patched breeches and shirts, etc. I have worn them myself in the last few weeks. I have not observed them on any of the gentlemen who advocated them publicly, and I will say I think it would be a good thing to get right down to that proposition.

I started to raise the farmers' objection to luxury taxes, and it is a fundamental one. If we do not buy the luxury you do not have the tax and you have a deficit. If you do buy the luxury you are wasting man power. That is a most radically illogical suggestion on the part of the Treasury, and I do not speak personally about Mr. McAdoo, but may I say that we should not waste the power of a single man or woman during this war? We have been looking over the fashion plates of the New York papers containing pages of advertising, asking people to spend their money for luxuries and things that are utterly unnecessary. I was talking to a farmer the other day about it. He said, "My wife spends \$24 a year for clothes." I said, "Did you see the story of the New York woman who asked to be allowed \$20,000 a year for clothes?" It is not only the folly of spending that money for clothes, but it is the folly of employing anybody to make those clothes.

We have a serious proposition to win this war. After they get beyond the Rhine, we will have a big job. We have to conserve the man power of the country.

Senator SMITH. Are you a native of New York?

Mr. MARSH. No; I was not born in New York. I have lived there about 11 years.

Senator SMITH. Are you a native of the United States?

Mr. MARSH. My father and mother were native born. I happened to have been born in Bulgaria. My father and mother were Congregational missionaries.

Senator SMITH. What is your business?

Mr. MARSH. It has been stated in the record.

Senator TOWNSEND. What salary do you receive?

Mr. MARSH. I receive the munificent salary of \$3,600 a year.

Senator SMITH. From all the organizations?

Mr. MARSH. From all the organizations combined.

Senator THOMAS. Is that exclusive of your expenses?

Mr. MARSH. Well, my expenses for car fare, etc., amount to a few dollars a month.

Senator THOMAS. Well, I do not care whether they are large or small. Do you get your salary exclusive of your expenses?

Mr. MARSH. Yes.

Senator SMITH. They do not pay your hotel bills in Washington, do they?

Mr. MARSH. No, sir.

Senator SMITH. Do you live here?

Mr. MARSH. I live here with my family and pay my rent. Would it be in order for me to reciprocate and ask the Senators what their income is and where they get it?

Senator THOMAS. I will answer that question if you want me to.

The CHAIRMAN. Well, I do not think it is quite necessary. I do not think it is fair to either side.

Mr. MARSH. Why is it fair to ask me that? I am perfectly willing to tell. I have been offered two or three times that salary, and could have had several times that salary, to shut up and do nothing.

Are there any further questions?

Senator SMITH. My reasons for asking you where you were born was because I wanted to identify your connection with American life. It was not meant in any way except for that purpose, to show that you were really a citizen of New York and actually identified with American life.

Mr. MARSH. Yes, sir; I went through college at Grinnell, Iowa, and worked at farming. I have had three years in Chicago and Pennsylvania universities, and thank God I have been able to outlive it and really understand something about economics.

The CHAIRMAN. You are here properly representing what you regard as the interest of the farmers?

Mr. MARSH. I am here speaking officially for the organized farmers.

The CHAIRMAN. You are representing a very important interest of the country.

Mr. MARSH. I am representing an industry of the country which is on the "blink," let me add, Senator, and the farmers have got to be recognized as an essential industry, but the Congress of the United States will have to take some action pretty soon to change and improve conditions or the farmers can not do their share toward winning the war.

Senator JONES. Who is at the head of your organization?

Mr. MARSH. Hon. Arthur Capper, governor of Kansas, who, it is said, is going to join you shortly in the United States Senate. I

thank you, gentlemen; I did not mean to be personal, but when the personal question was put to me, recognizing the right of the American people, I thought we ought to have a fair show all around.

Senator THOMAS. I did not intend to be personal, in so far as that particular phase of it was concerned. I am perfectly willing to answer your question.

Mr. MARSH. May I ask the privilege of submitting this typewritten brief with the detailed figures in a day or two?

The CHAIRMAN. You may do that.

(The brief referred to above is here printed in full, as follows:)

BRIEF SUBMITTED TO THE SENATE FINANCE COMMITTEE REGARDING THE PENDING REVENUE BILL BY THE FARMERS' NATIONAL COMMITTEE ON WAR FINANCE.

[Gov. Arthur Capper, chairman; Hon. Herbert F. Baker, vice chairman; Benjamin C. Marsh, executive secretary. Bliss Building, Washington, D. C.]

COST OF THE WAR.

If the war continues through or even well into 1920 the total money cost to this country will be probably about \$100,000,000,000. This includes loans to our allies, which they may not be able to repay and which we may not want them to repay, interest on the debt, and a very small amount for pensions. It is of the utmost importance, therefore, that we should adopt sound principles of securing revenue which will enable us not only to finance the war adequately but which will leave the country in the best condition after the war, and in a position to recover its economic and industrial status as soon as possible.

THE PRINCIPLES OF THE REVENUE BILL.

The following principles should control in the drafting of the revenue bill:

1. To secure adequate revenue equitably.
2. To increase production.
3. To prevent waste.

It is our judgment that this involves a complete readjustment and that the only way in which these three essentials to a just revenue bill can be carried into effect is through the principle of equality of financial sacrifice.

The national income for 1914 from wages, salaries, rent, dividends, interest, profits, etc., was conservatively estimated at \$33,000,000,000, for 1916 at \$50,000,000,000, for 1917 at sixty-three to sixty-four billions, and the income for this year (1918) is estimated approximately \$72,000,000,000. The national income this year will therefore be about \$39,000,000,000 larger than the national income in 1914. The cost of the war in dollars and cents will be, during the coming year, about twenty-four to twenty-five billion dollars, according to the present estimates, exclusive of contract authorizations.

The problem of production is fully as important as the question of raising revenue, but it is obvious that since wholesale prices are (June, 1918) approximately 90 per cent higher than in 1914, a marked reduction in domestic consumption is essential to enable us to secure the needed war revenue, whether by taxation or by loans. Probably three to three and a half million people, who in 1914 were supported out of the individual earnings or income which totaled the national aggregate income of thirty-three billions, will be maintained out of the appropriations for the war this year. Therefore the total population to be supported out of the national income of about seventy-two billions, exclusive of the cost of the war, will be somewhat less than the number that was so supported in 1914, with a national income of about \$33,000,000,000. If properly distributed, the national income in 1914 would have been fairly adequate for the national needs, and during that year large sums were laid aside for investment. The savings to conduct the war must amount, therefore, to approximately five-eighths of the increase in the national income in 1918 over that of 1914, whether these savings be taken in taxes or as loans. In 1917, with an estimated income of sixty-three to sixty-four billion dollars, it was estimated that between eighteen and nineteen billion dollars were saved for investment, Federal taxes, etc. This sum must be increased this year, to

enable us to finance the war, by at least between five and six billion dollars. It is therefore imperative that additional saving should be effected through reducing consumption and refraining from increasing capital investment in houses, machinery, etc., and through saving in personal expenditure.

THE NATIONAL INCOME IN 1916.

The Bureau of Internal Revenue reports the following facts:

(a) *Personal income*.—The total net income of the 437,036 persons making returns (including 7,635 married women making separate returns) as having incomes of \$3,000 and over was \$5,298,577,620.

Of this amount only \$2,572,027,890 was subject to the normal income tax and \$1,043,310,000 was exempted, as a specific exemption, and \$2,136,468,625 as dividends.

The gross income of the 437,036 persons making returns was \$8,349,901,983 and the general deductions amounted to \$2,051,324,363.

The gross income from personal service and business amounted to \$4,488,751,296 (p. 53), 76 per cent of the total gross income.

The total income from property was \$3,861,150,687, divided as follows:

Rents	\$601,919,604
Interest on notes, bonds, and mortgages	667,566,370
Fiduciaries	379,795,249
Royalties	41,883,053
Incomes from foreign sources	33,517,780
Dividends	2,051,324,363

Total earned and unearned income..... 3,861,150,687

There were 157,149 returns of incomes of \$3,000 to \$5,000—35.95 per cent of the total number of returns. The gross income of this group was \$956,229,497, divided as follows:

Income from personal service and business	\$703,516,995
Income from property	252,712,502

the percentages being, respectively, 73.57 per cent and 26.43 per cent.

There were 249,556 returns of incomes from \$5,000 to \$40,000, or 57.10 per cent of the total number of returns. The gross income of this group was \$3,980,547,895, divided as follows:

Income from personal service	\$2,396,417,828
Income from property	1,584,130,069

the percentages being, respectively, 60.20 per cent and 39.79 per cent.

There were 22,600 returns of incomes of \$40,000 up, including the incomes of millionaires, or 5.19 per cent of the total number of returns. The gross income of this group was \$3,413,124,591, divided as follows:

Income from personal service	\$1,388,816,475
Income from property	2,024,308,116

the percentages being, respectively, 40.69 per cent and 59.31 per cent.

It will be noted that only 26.43 per cent of the gross income of those receiving incomes of \$3,000 to \$5,000 was from property, while this income was 39.79 per cent of the incomes of \$5,000 to \$40,000 and 59.31 per cent of incomes over \$40,000.

It is a well-recognized principle that unearned income should be taxed higher than earned income, and since incomes of over \$40,000 are chiefly unearned or due to some conspicuous ability which will not be exterminated by heavy taxation for a few years, obviously the rate of taxation upon incomes of over \$40,000 should be very heavy, at least 60 per cent to 70 per cent of the total income.

The class having the largest aggregate income in 1916 were capitalists, investors, and speculators, of whom there were 85,465 making returns. Their total income was \$1,679,228,016 and their average income \$19,645.79.

The largest average income was secured by mine owners and mine operators, of whom 2,544 made returns—that is, 17.88 per cent of the total number of owners and mine operators in the country. Their average income was \$45,317.92. Of this group, 413 received incomes of \$50,000 to \$500,000, 8 received incomes of \$500,000 to one million, and 11 received incomes of over one million.

The 2,839 stock and bond brokers—20.68 per cent of the total number of such brokers—received an average income of \$41,009.27, and a total income of

\$116,425,299. Five hundred and twenty-three stock and bond brokers received an income of \$50,000 to \$500,000, 16 an income of \$500,000 to one million, and 9 an income of over one million.

AGRICULTURISTS.

The census of 1910 (used by the Bureau of Internal Revenue for occupational distribution of population) reports that there were in that year 6,047,615 agriculturists—farmers, stock raisers, orchardists, etc.—in the country. In 1916, 14,407 of these made returns under the income-tax law—that is, 0.24 per cent (less than one-quarter of 1 per cent of the total number). Their total income was \$129,642,432; their average income \$8,998.57. Of this number, 245 had an income of \$50,000 to \$500,000, 9 of \$500,000 to one million, but not one an income of over one million.

WHAT OCCUPATIONS ARE MOST PROFITABLE.

The Commissioner of Internal Revenue gives the following percentages in various occupations, taking the number of persons as per census of 1910, who filed returns in 1916:

	Per cent filing returns.
Architects.....	8.54
Authors, editors, reporters, etc.....	6.53
Clergymen.....	1.42
Engineers—civil, mining, etc.....	11.24
Lawyers and judges.....	18.97
Medical profession: Physicians, surgeons, oculists, dentists, nurses, and other medical specialists.....	6.97
Public service—civil.....	.78
Public service—military.....	7.08
Theatrical profession: Actors, singers, musicians, etc.....	.55
Teachers: From kindergarten to university, also school and college officials.....	.47
Agriculturists: Farmers, stock raisers, orchardists, etc.....	.24
Real estate brokers: Agents and salesmen.....	4.88
Stock and bond brokers.....	20.68
Brokers: All other.....	20.77
Commercial travelers.....	4.57
Insurance agents and solicitors.....	8.19
Lumbermen.....	10.76
Manufacturers.....	10.05
Merchants and dealers: Storekeepers, jobbers, commission merchants, etc.....	4.36
Mine owners and mine operators.....	17.88
Saloon keepers.....	1.92
Theatrical business: Owners, managers, etc.....	2.58
All other business.....	18.26

B. Corporate income.—The gross income of the 341,253 corporations reporting for 1916 was \$35,327,631,015, the net income \$8,765,908,984. The main divisions and net income of each were:

Agriculture and animal husbandry.....	\$69,862,431
Extraction of minerals.....	798,883,349
Manufacturing and mechanical industries:	
Food and kindred products.....	329,622,002
Textiles and their products.....	383,111,197
Iron and steel products.....	1,129,416,965
Lumber and its manufactures.....	114,683,677
Leather and finished products.....	137,134,060
Paper and printing.....	212,764,655
Liquors and beverages.....	83,150,751
Chemicals and allied products.....	604,351,657
Stone, clay, and glass products.....	88,357,208
Metals and metal products other than iron and steel.....	565,362,713
Miscellaneous industries.....	410,661,076
Public utilities.....	1,541,076,180
Banks and insurance companies.....	328,505,811
Merchandising companies.....	404,875,807
Miscellaneous companies.....	1,205,079,556
Total.....	8,765,908,984

C. Personal income tax paid.—The total normal tax paid by those making returns in 1916 was \$51,440,558. The total additional tax (super tax, etc.) amounted to \$121,948,136, a total of \$173,388,694.

The average rate of tax on incomes of under \$5,000 was less on incomes of \$4,000 to \$5,000 than on incomes of \$3,000 to \$4,000, being, respectively, 0.204 per cent and 0.289 per cent. The rate on incomes of \$15,000 to \$20,000 was only 0.934 per cent, and the rate on incomes of \$5,000,000 and over was only 12.908 per cent—the average rate on all incomes taxable being 2.753 per cent.

D. Taxes paid by corporations.—The total normal tax paid by corporations showing a net income in 1916 was \$171,805,150, divided as follows:

Agriculture and animal husbandry.....	\$1, 376, 651
Extraction of minerals.....	15, 846, 557
Manufacturing and mechanical industries.....	81, 260, 749
Public utilities.....	30, 160, 766
Banks and insurance companies.....	10, 505, 529
Merchandising companies.....	9, 037, 152
Miscellaneous companies.....	23, 617, 746
Total.....	171, 805, 150

The total national income in 1917 was estimated at sixty-three to sixty-four billions.

A. Personal income.—It is estimated that for 1917, there were about three and a half million tax returns under the reduction of exemption from three and four thousand dollars to one and two thousand, respectively, and that the total income was approximately twelve billion dollars, of which four to five billion was subject to the normal income tax and two and a half billion to three billion was not subject to the normal income tax because it was received from dividends.

B. Corporate income.—The total corporate income in 1917 is estimated at approximately \$10,450,000,000, divided roughly as follows, among the five large classes of corporations or industries:

Financial.....	\$690, 000, 000
Public service.....	1, 500, 000, 000
Industrial.....	6, 500, 000, 000
Mercantile.....	620, 000, 000
Miscellaneous.....	1, 200, 000, 000
Total.....	10, 450, 000, 000

The Treasury Department has prepared a statement comparing the net income of 240 industrial corporations in 1917 and in 1916. These are widely distributed as follows:

Net income, dividends, and surplus for 240 industrial corporations, years 1917 and 1916.

(000 omitted.)

Item.	Number of corporations.	Net income.		Dividends.		Surplus.	
		1917	1916	1917	1916	1917	1916
Powder.....	1	\$49,113	\$82,013	\$33,671	\$62,502	\$15,442	\$19,504
Arms.....	4	13,082	25,585	2,412	9,259	10,671	16,326
Automobiles.....	13	75,381	74,879	22,689	25,530	52,692	49,349
Gold mining.....	6	2,327	4,099	3,513	3,425	1,196	675
Copper.....	31	122,030	164,806	74,184	70,361	38,846	104,441
Rubber.....	7	41,548	24,034	11,511	8,700	30,037	15,334
House furnishings.....	1	509	1,802	.....	.....	59	1,802
Nondurable goods.....	5	17,060	12,499	6,324	5,162	10,736	7,337
Locomotives.....	7	35,909	25,019	12,351	8,661	23,558	16,358
Ships.....	3	6,509	8,146	2,742	4,877	3,767	3,299
Machinery.....	15	66,567	54,687	25,270	22,742	41,297	31,945
Agricultural implements and miscellaneous.....	7	24,327	16,718	7,788	6,498	16,539	10,220
Type.....	1	790	925	539	450	251	475
Paper.....	6	16,579	6,895	2,965	1,839	12,614	5,056
Iron and steel.....	19	707,296	440,878	168,303	94,647	538,994	345,231
Snuff.....	1	918	1,079	840	840	78	239
Licorice.....	1	218	365	180	190	38	175
Tobacco.....	8	36,468	31,396	25,445	24,982	11,023	6,414
Realty.....	1	493	601	.....	.....	493	601
Department stores.....	3	30,387	26,933	11,926	10,508	18,461	16,427
Mail order and miscellaneous.....	6	14,795	12,192	5,600	3,114	9,175	9,078
By-products.....	1	3,460	4,248	1,460	2,360	2,000	1,858
Coal.....	6	24,068	8,271	8,376	4,686	15,692	3,585
Fertilizers and chemicals.....	4	22,603	23,520	7,116	5,690	15,487	17,829
Cottonseed oil.....	2	3,682	3,505	1,924	1,421	1,758	2,084
Paint.....	1	4,897	2,978	2,738	2,532	2,159	446
Petroleum products and refining.....	23	210,641	153,364	54,467	40,030	156,174	113,234
Foods.....	23	178,828	123,719	45,594	37,054	133,234	86,665
Building materials.....	7	16,005	10,108	4,738	4,687	11,267	5,421
Clothing.....	6	16,660	11,920	7,074	6,753	9,586	3,167
Collars.....	1	2,530	2,812	1,570	1,390	960	1,422
Shoes.....	2	2,737	2,372	1,312	792	2,425	1,580
Tin.....	3	22,221	10,148	3,681	3,640	18,540	6,508
Zinc, silver, and nickel.....	10	27,540	14,249	22,083	31,174	5,457	13,078
Malt and beer.....	3	1,860	1,991	1,256	1,175	604	816
Liquors.....	2	17,606	7,873	5,096	1,716	12,510	6,175
Total.....	240	1,818,644	1,425,531	587,188	509,389	1,231,458	916,136

Of these groups of corporations only 12 of the 36 showed a smaller net income in 1917 than in 1916, but the total net income of these 240 typical industrial corporations was nearly \$400,000,000 greater in 1917 than in 1916, the figures being in 1917 \$1,818,644,000, and in 1916 \$1,425,531,000. The copper companies reported (31) showed a net reduction in 1917, the net income in 1917 being only \$122,030,000, as against \$164,806,000 in 1916. The price fixing of copper seemed to have an effect. Nineteen iron and steel corporations for which returns were given showed a large increase, the net income in 1916 being only \$440,878,000, and in 1917 \$707,296,000, an increase of about \$307,000,000.

TAXES.

It is estimated that the total income tax paid by all the corporations under the excess-profits tax for 1917 was \$1,691,000,000, while their war profits amounted to \$5,204,864,000. An 80 per cent tax on war profits would have yielded about \$4,163,000,000. The actual tax paid was equal to 32.5 per cent of the war profits, as follows:

	Per cent.
Financial.....	55.5
Public service.....	14.2
Industrial.....	33.9
Mercantile.....	90
Miscellaneous.....	24.5

SUGGESTED TAXES ON CONSUMPTION.

In the memorandum of "Possible sources of revenue," suggested by the Treasury Department and submitted to the Ways and Means Committee, the following statement is made;

"The retail-sales tax, however, raises a different set of considerations. That tax is recommended not only to raise additional revenue, but for the equally important purpose of discouraging wasteful consumption and unnecessary production. It would be superfluous at this stage of the war to dwell upon the fact that waste and extravagance are akin to treason. We pay lip homage to this truth, but we neglect its practice. We are not yet cutting our personal budgets sufficiently to make the excess of national production over national consumption equal to the needs of the Government. The retail-sales tax distinctly labels the taxed articles as luxurious and serves notice that the Government's ban is upon it."

The consumption taxes on nonessentials, suggested by the Treasury Department, would tend to defeat their own purpose. It is stated: "The retail-sales tax distinctly labels the taxed articles as luxurious, and serves notice that the Government's ban is upon it." In other words, the Government says that the purchase of the articles upon which this 20 per cent or higher tax is levied is, to quote the memorandum, "akin to treason." It would seem obvious that the Government should not compound a felony or even a misdemeanor by the payment of a 20 per cent tax, whether this tax is paid by the manufacturer or by the purchaser. The suggestion is an indirect and impracticable method of attempting to reduce consumption and secure revenue at the same time. We say "impracticable" on the basis of the experience of our allies, which have tried the system of taxation as shown in the pamphlet prepared by the Ways and Means Committee in the Legislative Reference Library of Congress entitled, "War Taxation of Incomes, Excess Profits, and Luxuries." Luxuries are manufactured, and the Government derives some revenue therefrom, but only a small proportion of the cost of the war, and our allies, mistakenly from a fiscal point of view, have relied upon these taxes, "indirect income taxes," instead of upon a direct income tax. They are raising only a very small proportion of the total current cost of the war by taxation.

In view of the fact that the United States is underwriting the entire financing of the war, it would be an egregious blunder, inexcusable in the light of our allies' experience, for us to attempt the same method of getting revenue. We ought to face the fact that in order to finance the war we have got to reduce consumption right down to the core; that men and women must not buy clothing and furniture, nor a single one of the articles upon which the memorandum of the Treasury Department suggests a retail tax or specific tax, unless these articles are absolutely needed. The suggestion about "padding" revenue by requiring manufacturers or merchants to give bonds is not feasible. We must eliminate the manufacture of all nonessentials. The Government has got to go through the factories of the country with a fine-tooth comb, and take out the men who have had training on farms and place them back on the farms, or else we shall be in imminent danger of losing the war through starvation. Hundreds, if not thousands, of nonessential factories must be shut down, including unquestionably factories manufacturing goods on the lists suggested by the Treasury Department, and this, at least, for the period of the war, and possibly for a longer time.

If we reduce consumption sufficiently to raise twenty-four to twenty-eight billion dollars for the cost of the war, whether by bonds or by taxes, very few of the articles or commodities suggested for taxation in this memorandum would be purchased, and the revenue therefrom would be negligible.

A detailed analysis of the list shows this fact plainly. Some watches have got to be bought. A tax of 50 per cent thereon is exorbitant if people need watches. If not, a tax of 500 per cent would be just as reasonable. There is no excuse for manufacturing jewelry during the war, and such manufacture can not be made patriotic by a 50 per cent tax. No automobiles, motor cycles, and bicycles, including parts and accessories and tires, should be manufactured during the war for pleasure purposes. The Treasury Department and the Fuel Administration seem to be working at cross purposes, inasmuch as the Fuel Administration has reduced the coal allotment for factories making pleasure automobiles to 25 per cent of the normal quantity consumed. Musical

instruments, while essential in peace times, are completely nonessential during the war, except for military purposes. The manufacture thereof should be stopped, and those engaged in the manufacture thereof put to work to help win the war. Obviously, no liveries should be manufactured during the war. Congress should not only tax the butler out of the pantry, but the coachman off the box.

The proposed tax upon house furnishings must be criticized similarly. People do not need to buy ornamental lamps and fixtures, fancy articles, and knick knacks during the war. We have a large supply on hand! If they do need curtains or carpets or rugs, as in the case of clothing, it is better economy to purchase a substantial wearing one than poor ones which are more expensive in the long run. It is difficult to comprehend the mental processes of those who suggest a tax upon cutlery—the serviceable kind—and upon purses, brushes, combs, and other toilet articles of reasonable necessity; also a tax upon furniture costing more than \$5 per piece. It is not considered a crime to marry and raise children, and those who marry will have to buy furniture. Why they should be taxed thereon, if they buy only what they need, is inexplicable. Chinaware, or some sort of tableware is a necessity; cut glass a luxury. Yet, these are put in the same class in the suggestion to the Ways and Means Committee.

A study of the proposed taxes upon soft drinks, chewing gum, etc., raises the question as to why the Food Administration and the Treasury Department do not get together. The Food Administration has suggested the elimination of soft drinks as far as possible, as consuming sugar, of which we are short. The Treasury Department would seem to throw the mantle of patriotism over the unpatriotic consumption of sugar by taxing its use in these beverages. We can probably survive the period of the war without great indulgence in perfumes and cosmetics.

The United States will probably take a lesson from the British Labor Party and realize the necessity of complete prohibition during the war. A tax upon denatured and wood alcohol would be a most vicious burden upon the farmers of the country. The suggested tax upon tobacco in its various forms is the most nearly excusable tax suggested, but the situation could be better met by eliminating the tobacco industry for the period of the war, except in so far as the Government needs it for men in the service. The suggested tax of 10 cents per gallon on gasoline, levied on the wholesale dealer, is an admission either that the wholesale dealer is profiteering unconsciously, in which case he can be reached by a war-profits tax, or that some further discouragement on production is due the farmers and other producers. A tax upon automobiles, if applicable, as is not clear from the context, to trucks, is an inexcusable burden upon production. The license tax on a Ford car of \$15 will, of course, affect very largely the farmers of the country who use these cars for business and to save horses; that is, to save feed. They do very little pleasure riding.

The doubling of the tax on admission to amusements seems unjust, because there is no exception. The Treasury Department evidently has overlooked the fact that the majority of the families of the country have an income of less than \$1,500, and that their recreations are cheap because they have to be.

The tax on yachts, pleasure boats, power and motor boats seems to compromise the Government, since those propelled by gasoline and by coal use essentials which the working people and the poorer classes are asked to conserve, and which all should conserve. The payment of even a large tax should not grant license to those who can indulge in conspicuous consumption to waste material needed for the winning of the war. The suggested tax upon servants will produce little revenue but many liars, since it can be evaded. The only effective way to prevent extravagance and the consumption of nonessentials and luxuries is not through the system suggested by the Treasury Department but through the absolute prohibition of the manufacture and production of nonessentials and the transformation of factories producing such nonessentials and luxuries into war service and those employed therein into similar help in winning the war. Sufficient revenue can be secured by heavy taxes on incomes, on war and excess profits, and on the value of unused and inadequately used land. The collection of taxes suggested by the Treasury Department would involve the services of two or three Army divisions which might better be employed in production necessary for the winning of the war.

How \$12,500,000,000 can be raised for the fiscal year ending June 30, 1919, twelve billions for the war and half a billion for ordinary Federal expenditures, exclusive of Army and Navy, in 1919:

War-profits tax.....	\$3, 875, 000, 000
Income tax.....	6, 000, 000, 000
Corporation tax.....	555, 000, 000
Customs.....	230, 000, 000
Tax on the value of unused and inadequately used land.....	500, 000, 000
Miscellaneous.....	1, 321, 215, 000
Total.....	12, 481, 215, 000

Twenty-four to twenty-eight billion dollars must be raised during the current fiscal year for the cost of the war, by loans or taxes. Since this has got to be done, half of this sum can be raised by taxation if Congress determines to do so. It resolves itself into a question of whether the Government shall borrow from those of small means and tax those of comfortable and enormous incomes, or borrow chiefly from the well-to-do, and tax the workers.

1. The war-profits tax: The war profits—that is, the profits over the three-year prewar period—were, last year, approximately \$5,295,000,000, as shown above. Had we levied a war tax of 80 per cent, we would have secured approximately \$4,163,000,000, instead of the proceeds of the excess-profits tax—about \$1,691,000,000. In other words, we would have secured about \$2,472,000,000 additional.

The estimated net income of corporations for the present year is \$9,600,000,000, divided as follows:

Financial.....	\$600, 000, 000
Public service.....	1, 400, 000, 000
Industrial.....	5, 900, 000, 000
Mercantile.....	600, 000, 000
Miscellaneous.....	1, 100, 000, 000

The income subject to a war-profits tax is approximately \$4,305,000,000, divided roughly as follows:

Financial.....	\$80, 846, 000
Public service.....	286, 701, 000
Industrial.....	3, 230, 980, 000
Mercantile.....	90, 160, 000
Miscellaneous.....	636, 169, 000

Ample deduction having been made, it would seem perfectly reasonable to levy a tax of 90 per cent upon these war profits, which would yield \$3,875,000,000.

2. Personal income: The personal income last year was estimated at \$12,000,000,000, of which four to five was subject to the normal income tax, and two and a half to three billions was not subject because dividends. The personal income for 1918, with the exemption, as in 1917, of only one and two thousand dollars, respectively, will be approximately \$14,000,000,000, from which three and a half billions should be deducted as dividends. This income of about eleven and a half billions received by approximately two and a half million families and individuals averages \$4,600 per family. In 1916, approximately 5,530 families or individuals received each a net taxable income of over \$100,000. Had the Government taken in 1917 all net incomes in excess of \$50,000, the Government would have secured from this group, in round figures, a total of \$1,519,535,000; a moderate tax rate on the net incomes of \$3,000 to \$100,000 would have yielded \$1,520,430,000, a total of \$3,039,965,000:

All incomes in excess of \$50,000.....	\$1, 519, 535, 000
Moderate tax on incomes from \$3,000 to \$100,000.....	1, 520, 430, 000
Total.....	3, 039, 965, 000

The rates would have been an average of—

10 per cent on the net income of those receiving from.....	\$3, 000 to \$4, 000
12 per cent on the net income of those receiving from.....	4, 000 to 5, 000
20 per cent on the net income of those receiving from.....	5, 000 to 10, 000
25 per cent on the net income of those receiving from.....	10, 000 to 20, 000
40 per cent on the net income of those receiving from.....	20, 000 to 40, 000
50 per cent on the net income of those receiving from.....	40, 000 to 60, 000
70 per cent on the net income of those receiving from.....	60, 000 to 80, 000
75 per cent on the net income of those receiving from.....	80, 000 to 100, 000

These figures are, of course, average, and could be adjusted to ranges of income within the ranges noted.

In 1918 the total net income of those liable to the income tax was, in round figures, \$6,300,000,000, an increase of \$1,700,000,000 over the net income in 1915. Assuming, as it is conservative to do, a similar increase for the two years 1917 and 1918, the total net income of those receiving \$3,000 and over is about \$3,500,000,000 greater in 1918 than in 1916, so that the rate of taxes suggested would have yielded nearly three-fifths more than in 1916, or approximately \$1,800,000,000, a total of about \$4,840,000,000.

There were about three and a quarter million individual income-tax returns for 1917. Of this number probably at least 175,000 received net incomes of two or three thousand dollars, or approximately a total net income of about \$5,000,000. A tax of 8 per cent on this net income would yield roughly \$40,000,000, a total from these groups of \$4,880,000,000. Obviously, the 19,000,000 families and individuals of the United States who did not make tax returns could pay an income tax of \$1,120,000,000, or an average of about \$58 per family. This totals \$6,000,000,000 from the income tax.

It must be remembered that the exemption in all of our allies is very much lower than in this country, and that the rates in Great Britain on incomes of \$100,000 or less are much higher than in the proposed revenue bill. Full data on this point is given by the Ways and Means Committee in their report on the revenue bill of 1918 (No. 767, 65th Cong., 2d sess.).

These figures are admittedly approximate, and necessarily so, because full data is not yet available in the Bureau of Internal Revenue. That six billion dollars can be raised by direct income taxes is, however, self-evident. The base and range of incomes can be determined approximately from the information in possession of the Commissioner of Internal Revenue, and the rates adjusted accordingly.

While it seems drastic to take all incomes in excess of \$50,000 from those who have incomes of \$100,000 or over, and to tax incomes in excess of \$40,000 as heavily as suggested, this is entirely justifiable since, as the figures quoted from the Commissioner of Internal Revenue above show, nearly three-fifths of incomes of over \$40,000 come from property; that is, are unearned incomes and therefore may properly be subjected to a very much heavier tax rate than incomes from personal exertion. The huge income from war industries, not all of which can be reached by the war-profits tax, should equally be subjected to such a heavy tax. The rates suggested for the personal income tax will in large measure prevent foolish expenditure. It is true that since earnings are received during the present year and the tax paid next year, people do not have the same incentive to save to pay their income tax, but this objection would lie as well against the taxes on consumption which have been suggested.

The administration might well conduct a nation-wide campaign immediately to make people know that they have got to pay a large proportion of their incomes of over \$10,000 as taxes, and with the imposition of the tax rate suggested there will be no difficulty in getting people to subscribe all they can to the liberty loan. To win the war the whole national income has got to be socialized. To the objection raised against such drastic taxation, which is mis-called "confiscation," that it will prevent expansion of industry, and deter men of conspicuous ability from large production during the war, the answer is clearly that there should not be any expansion of business, except that which is necessary for the winning of the war, which will be financed by the War Finance Corporation, and that the gentlemen of conspicuous executive and business or financial ability who decline to cooperate with their Government through rendering the service they are best fitted to render during this emergency put themselves in the class of the unpatriotic.

Strictures on profiteering are not in order at present because those who take the risks of production are entitled to a monetary return immediately which will enable them to protect themselves from any possible loss, and these profits can be adequately covered into the Public Treasury through war profits and income taxes.

The failure to adopt this point of view, as far as the farmer is concerned, has brought about the most serious menace in the whole war situation—the supply of food.

The figures of the yield of the corporation tax, customs tax, and miscellaneous taxes are taken from the Secretary of the Treasury's estimate of the receipts for the fiscal year 1919 under these headings.

It is obviously constitutional for Congress to levy an excise tax upon the privilege of holding land unused or inadequately used. If there were any question on this point it can be resolved in favor of the proposition by reference to the fact that the Congress can pass a law taxing the value of unused and inadequately used land, and provide therein that the Supreme Court shall not have jurisdiction with respect thereto, as provided in the Constitution of the United States. The value of unused or inadequately used land in the United States is conservatively estimated at \$25,000,000,000. The value of unused and inadequately used land is, in New York City alone, approximately two and a half billion dollars. A tax of 2 per cent on the value of such land in the United States would yield about \$500,000,000, of which New York City would pay between forty-five and fifty million dollars.

By a remarkable oversight the revenue bill proposed by the Ways and Means Committee entirely exempts owners of idle lands held for speculation, and essential to the early and most economic winning of the war, despite the fact that the enormous war expenditures are materially increasing the value of their holdings.

The above outline shows incontrovertibly how twelve and a half billion dollars can be secured for the Federal Government during the present fiscal year.

A tax on advertising under the same scheme is entirely unnecessary if the suggestions above be adopted, and all publishers making money from their advertisements or otherwise, will be compelled to pay their full share of the cost of the war through the few obvious, direct, and honest taxes we recommend. It will be noted that we have suggested an administrative matter of great importance not only from economy of administration but from the point of view of securing revenue, to wit, that there should be a flat tax levied on incomes instead of a series of graded taxes.

We make in conclusion the following specific recommendations:

1. Make it a criminal offense not to give the real equitable ownership of stocks in corporations and business concerns.
2. Compel all corporations and business concerns to declare dividends and prohibit the issuance of stock to conceal earnings.
3. Provide for full publicity as to incomes of over \$25,000.
4. Levy flat instead of graded rates.
5. Tax unearned incomes from secure investments more heavily than incomes earned by labor.
6. Initiate a policy of greater reliance upon income taxes rather than upon taxes on corporations, excess, and war profits.

[By Gov. Arthur Capper, chairman Farmers' National Committee on War Finance. Published in the Farmers' Open Forum.]

The financial interests of the country are conducting a wide campaign to defeat the desire of the President and of democratic people of the United States, including farm and labor organizations, to have at least half of the cost of the war financed by current taxation. A press campaign is being conducted to prevent the war from being financed democratically. Papers like the New York Times are trying to make it appear that it would be difficult, if not impossible, to raise even \$8,000,000,000 by taxation during the present fiscal year ending June 30, 1919. It would be very much better to have Congress enact the revenue bill before the new loan drive, which is to start, according to the announcement by Secretary McAdoo, on September 28. It is expected that the fourth liberty loan will be for \$8,000,000,000, but in its issue of August 1 the New York Times says:

"Whether amount (of loan) is to exceed \$6,000,000,000 depends on tax bill being prepared. * * * The difficulties encountered in increasing the volume of taxation are recognized to be so great that Congress may decide on an adjustment of the load so as to require a larger bond issue than would otherwise be necessary."

THE FARMERS' NATIONAL COMMITTEE ON WAR FINANCE SHOWS THAT AT LEAST TWELVE BILLIONS CAN BE RAISED BY TAXES.

The Farmers' National Committee on War Finance submitted an elaborate brief to the Ways and Means Committee showing that nearly \$12,500,000,000

could be raised by current taxes during the present fiscal year without any injustice to any producer or any business. The chief sources of revenue are as follows:

War-profits tax	\$3, 875, 000, 000
Income tax	6, 000, 000, 000
Corporation tax	555, 000, 000
Customs	230, 000, 000
Miscellaneous	1, 321, 215, 000
Tax on the value of unused and inadequately used land	500, 000, 000
Total	12, 481, 215, 000

These estimates of revenue were based upon estimates of war profits and incomes, and were obtained in part from official sources not yet made public and from official documents such as the Secretary of the Treasury's estimate.

WHERE FARMERS AND CITY LABOR STAND.

The National Grange, the Washington State Grange, and the American Federation of Labor in their last annual meetings adopted resolutions which speak for themselves, as follows:

THE NATIONAL GRANGE.

"Therefore be it resolved that we call upon Congress, in the new revenue bill, to increase the tax on war profits to at least 80 per cent of such excess profits; to increase the surtaxes on all large incomes until all incomes over \$100,000 are taxed into the Nation's war chest."

THE WASHINGTON STATE GRANGE.

"Therefore be it resolved that we demand that the Congress of the United States insist that equality of financial sacrifice be enforced in paying for this war; that at least two-thirds of the cost of the war be paid by heavy taxes upon excess profits, upon unearned incomes, upon inheritances, and upon land values, and that no additional taxes be laid upon the consumers of the country to pay for this war, but that these taxes be continued until the entire cost of the war has been met."

THE AMERICAN FEDERATION OF LABOR.

"Resolved, That the American Federation of Labor urges Congress to levy taxes on war profits, swollen incomes, and on land values to an extent that during the period of the war will provide by taxation at least 50 per cent of the expenditures of the Government in any one year."

CREDIT MONOPOLY OR DEMOCRATIC TAXATION.

The set which monopoly has made to increase its size and its grip during the war is well illustrated in this campaign.

Monopoly of credit and consolidation of banking facilities have been proceeding very rapidly during the war, not only in America but in England and Germany. Mr. Richard Spillane, in a recent issue of Commerce and Finance, states that while at the close of the year 1916 there were only two banks in the world with deposits in excess of \$1,000,000,000, now there are at least four and possibly six, and London has three of them. He states that the London City & Midland Bank has now deposits of \$1,392,000,000; Lloyds, \$1,200,000,000; Imperial Bank of Germany (reported), \$1,167,000,000; the National City Bank, \$681,000,000; and the Guaranty Trust Co., of New York, \$500,000,000. Both the National City Bank and the Guaranty Trust Co. have increased their deposits largely in the last 18 months.

CONTROL OF MONEY AND CREDIT.

The Pujo Investigating Committee on Control of Money and Credit in its report made five years ago gives the opinion of some big bankers of the country on the concentration of control of money, as then developed. Mr. George McClelland Reynolds, president of the Continental & Commercial National Bank of Chicago, discussing the question, said:

"I am inclined to think that the concentration, having gone to the extent it has, does constitute a menace. I wish again, however, to qualify that by

saying that I do not mean to sit in judgment upon anybody who controls that, because I do not pretend to know whether they have used it fairly or honestly or otherwise."

Mr. Jacob H. Schiff, of Kuhn, Loeb & Co., made it clear that he was so near the top of the credit pile that concentration of money control did not worry him, as the following excerpts from his testimony show:

"Q. Now, confining yourself to the question of actual practical control of the management of these great moneyed corporations, you have observed, have you not, a growing concentration of control?

"Mr. SCHIFF. I have.

"Q. And has it been a subject of concern to you?

"Mr. SCHIFF. No; it has not.

Mr. George Fisher Baker, president of the First National Bank of New York, testified as follows:

"Q. I suppose you would see no harm, would you, in having the control of credit as represented by the control of banks and trust companies still further concentrated? Do you think that would be dangerous?

"Mr. BAKER. I think it has gone about far enough.

"Q. You think it would be dangerous to go further?

"Mr. BAKER. It might not be dangerous, but still it has gone about far enough. In good hands I do not see that it would do any harm. If it got into bad hands it would be very bad.

"Q. If it got into bad hands, it would wreck the country?

"Mr. BAKER. Yes; but I do not believe it could get into bad hands."

The Pujo Investigating Committee made the following statement:

"The resources of Morgan & Co. are unknown. Its deposits are one hundred and sixty-three million."

The committee showed, however, that the resources of the banks directly connected with Morgan & Co. are \$1,600,000,000, "aside from the vast individual resources of Messrs. Morgan, Baker, and Stillman," to which must be added the resources of the Equitable Life Assurance Society, controlled through stock ownership of J. P. Morgan & Co., amounting to \$504,000,000. This makes a grand total of \$2,104,000,000, nearly \$100,000,000 more than the actual money in circulation in the United States three years ago, and close to one-thirtieth of the total national income now. These figures, it must be remembered, are nearly six years old. No one knows what the financial resources and grip of these big banking concerns is to-day. It is noteworthy, however, that the National City Bank has just given a good character to the packers!

SHALL THE MONEY CONTROL, OR THE PRESIDENT AND THE PEOPLE OF THIS UNITED STATES DETERMINE OUR POLICY FOR FINANCING THE WAR?

The issue has been so clearly joined that he who runs may read. The following table of the national debt and percentage of the national wealth of the larger belligerents is very significant:

	Present national debt.	Per cent national wealth.		Present national debt.	Per cent national wealth.
Great Britain.....	\$31,156,000,000	34.6	Japan.....	\$1,300,000,000	4.6
France.....	23,000,000,000	35.4	Germany.....	31,000,000,000	38.7
Russia.....	25,400,000,000	68.5	Austria-Hungary.....	20,000,000,000	80.0
Italy.....	7,000,000,000	28.0	United States.....	12,000,000,000	4.8

It will be noted that, excluding Japan, the national debt of the United States is the smallest per cent of national wealth. It is only about one-sixth as large a proportion of the national wealth as that of Italy and less than one-eighth as large a proportion as that of Great Britain. Selfish financial interests ignore the fact that the settlement of national debts after this war presents a problem more difficult than beating the Kaiser. This latter is assured. We are going to do it. A big national debt is a dead weight on a nation's progress and will rest in chief measure upon the farmers of the country, who must pay the larger part of it. This is clearly the intention of the undemocratic selfish financial group of this country which seek to-day, as ever, to dominate not only the domestic but the foreign policy of the United States. What will be the answer of the farmers of America? They must make it heard promptly and unmistakably.

The CHAIRMAN. The committee will now hear from Mr. John H. Dieckman.

BROKERS.

STATEMENT OF MR. JOHN H. DIECKMAN, PRESIDENT OF THE ST. LOUIS STOCK EXCHANGE.

Mr. DIECKMAN. Mr. Chairman and gentlemen, my associates are here from New Orleans and Cincinnati. The gentleman from Cincinnati had to go back home last night, but asked me to introduce his remarks. We want to thank you for giving us this hearing this morning.

You are familiar with this clause in the bill. You had some testimony on that score, I believe, yesterday morning. We should have been here, and we were here, but a little bit late. We were two or three hours late coming in on the Pennsylvania. I do not know whether that is due to the new railroad management or not, but we were late just the same.

Speaking in behalf of the St. Louis Stock Exchange, I wish to state that the clause in this bill that fixes a license on each broker of \$100 and an additional tax if he is a member of a stock exchange, we feel, so far as the St. Louis Stock Exchange is concerned, that it is scarcely just in comparison with the schedule in this clause affecting other exchanges, such as New York, Boston, Chicago, and Philadelphia.

The total number of shares handled in St. Louis last year was one hundred and twenty-seven and odd thousand dollars—that is, for the entire year—on the floor of the St. Louis Stock Exchange. They handled more than that on the New York Stock Exchange in 10 minutes. The amount of bonds handled on our St. Louis Stock Exchange last year was one million six hundred and odd thousand dollars. You know what they handle in New York.

Senator SMOOT. How much in stock?

Mr. DIECKMAN. 127,000 shares of stock, all told. I will leave some figures with you. I have the printed pamphlet of our regular records. Here is the record for last year gotten up by the exchange: Total number of shares, 128,478, the market value of which was \$3,862,263.99. The total amount of bonds sold was 1,656,240, the value of the same being \$1,127,601.80; total bonds and stocks, \$6,989,865.79.

Now, you can very easily see, gentlemen, that under those conditions—under the limited number of transactions, both in number of shares and bonds—our market value, traded in our floor, when you tax us practically the same as they do the larger exchanges, it is altogether out of line. In fact, it is so much out of line, so far as it affects the St. Louis Stock Exchange and the New Orleans Stock Exchange, that it is prohibitive, as we look at it. It will, without any doubt, drive a number of the members of the St. Louis Stock Exchange and the majority of the other exchanges I have mentioned—Cincinnati and New Orleans—out of business, and may result absolutely in closing the exchanges.

Senator JONES. How many members have you?

Mr. DIECKMAN. We have in St. Louis a limited membership of 50.

Senator SMOOT. What business does a stock exchange do other than sell these few shares of stock?

Mr. DIECKMAN. The business of the stock exchange in St. Louis is largely one of quotations. We fix quotations there. We make a few trades such as I have outlined here, but we make quotations on a number of things that are hardly ever traded in, and they are a sort of guide to banks and trust companies where the question of loaning money on collateral is concerned.

Senator JONES. How can you make a quotation without a sale?

Mr. DIECKMAN. You can make a bid price, or there may be an asking price and there is not a transaction. The one is too low and the other is too high.

Senator JONES. But that is the way you fix prices?

Mr. DIECKMAN. Yes. One says we will give such a price, and the other says we will sell at such a price.

Senator JONES. I wanted to make it clear that you did not meet there and arbitrarily fix prices.

Mr. DIECKMAN. No; we do not. I want to say, gentlemen, that we do not do any business in the shape of future deliveries. What business we do transact on the floor of the exchange is regular and is for the next day's delivery; for cash, of course. We have no delivery 30 days or 60 days, like they have in New York or other places.

Senator SMOOT. Do you sell any grain upon your stock exchange?

Mr. DIECKMAN. No, sir; merely bonds and stocks. Our exchange is so limited in number and in volume of business—and I can say the same thing for New Orleans and Cincinnati—that the tax fixed in this bill is almost prohibitive. Our boys can not afford to pay it, that is all there is about it; that is, a good many of them can not afford to pay it.

The CHAIRMAN. The brokers' tax is \$100. Do you complain of that?

Mr. DIECKMAN. No; not specially. We are now paying a flat brokers' tax of \$30. You have increased that from \$30 to \$100 in the present bill.

The CHAIRMAN. It is not the \$100 tax that you are complaining of?

Mr. DIECKMAN. Not specially; but we complain of any tax, so far as the tax on membership is concerned, in our case. We are paying the tax to do business, and yet we are taxed again because we do some of that business on the floor, which is merely a medium through which we transact some of our trade.

The CHAIRMAN. I was trying to get at what part of this tax you object to. There is another tax in addition to that \$100. If the membership charge is \$2,000, you pay \$50 additional. If the membership charge is \$2,000 and not more than \$5,000, you pay \$100 additional. If the membership charge is above \$5,000, you pay an additional tax of \$150. Now, it is that tax particularly that you are objecting to, is it not?

Mr. DIECKMAN. We object to that. We object to the principle of it, for one thing, and we object, of course, to the amount fixed in the bill.

Senator SMOOT. Would you object to a tax based upon sales?

Mr. DIECKMAN. A tax on the sales on the floor?

Senator SMOOT. A tax based upon the sales made upon the floor.

Mr. DIECKMAN. Of course, that goes to the consumers.

Senator SMOOT. But would you object to that kind of a tax?

Mr. DIECKMAN. I do not see that we could very well object to it, Senator, because we are paying a transfer tax, a stamp tax, and all of those things.

Senator SMOOT. What I was getting at was this: You complain bitterly that the same rate of taxation should not apply to the St. Louis Stock Exchange as applies to the New York Stock Exchange on account of the volume of business done.

Mr. DIECKMAN. Yes.

Senator SMOOT. What I want to know is, would you object at all to a tax imposed upon the transactions made upon the exchange?

Mr. DIECKMAN. Personally, I would have no objection only so far as it might affect the volume of business by reason of an increased tax to the one who buys or sells.

Senator THOMAS. What are your seats worth?

Mr. DIECKMAN. Our last sale was \$1,000 plus the transfer fee, which goes to the exchange.

Senator THOMAS. And which is how much?

Mr. DIECKMAN. It is a mere nominal figure. They have sold higher, but that was some years ago. The last sale, as I have just stated, was at \$1,000. On this basis of tax we would have to pay \$50. There is New York, with a market value for its membership of \$55,000 or \$60,000, and they have to pay but \$150. You can clearly see the inconsistency there. Of course, the volume of business gives the membership a value. That is why our memberships are low, and our business is very limited.

Senator TOWNSEND. My question probably demonstrates the fact that I know nothing about stocks; but I want to ask you if the members of these stock exchanges get anything for making these quotations that you speak of?

Mr. DIECKMAN. On the floor; absolutely nothing.

Senator TOWNSEND. They make them for their own benefit?

Mr. DIECKMAN. Well, it sometimes happens, Senator, that a man has 100 shares of some bank or trust company's stock that has been dormant in the market. There has been no transactions in it, perhaps, not even a quotation, and he goes on the floor and makes a bid for it; or, if he has any to sell, he will fix a selling price in the hope of drawing out a bidder or a seller.

Senator TOWNSEND. That is, he goes in and does this in the hope of creating a market?

Mr. DIECKMAN. Yes.

Senator TOWNSEND. And it may be altogether a fictitious bid in the first place?

Mr. DIECKMAN. No; not fictitious.

Senator TOWNSEND. Well, you have a dormant stock and there has been no market for it for some time. You go on the stock exchange and offer that for sale at a certain price.

Mr. DIECKMAN. It very frequently happens that a broker gets an order to sell something for which there is no market; there is no bidder; or to buy something and there is no seller. You can put in your bid price or asking price, but you get no response from the other side, because there happens to be nothing going on—no one

either to buy from you or to sell to you. But most of the things that we trade in there are more or less active. It is only here and there that we have quite an array of stocks that are listed, but comparatively few that are traded in.

Now, there is another thing in this bill, Mr. Chairman, and that is this: It says here that a broker shall be taxed \$100; and if he is a member of a stock exchange, or if he is a member of any produce exchange, board of trade, or a similar organization, he shall pay an additional amount. We have brokers who are members of stock exchange and they are members of a merchants' exchange or board of trade or cotton exchange. Is that broker to be taxed for his membership in each one of these different exchanges? Or does it mean that he is to be taxed as a broker; and if he happens to be a member of the exchange, he is to be taxed so much, or does it mean that he is to be taxed in every exchange of which he is a member? It is all a part of the brokerage business. Now, I have a case in my office. We have a gentleman who has been in our office for 25 years, and he is a member of a stock exchange which was organized 25 years ago. There was an organization perfected, and the membership cost nothing, simply annual dues. Now, being an employee, we told him to take out the membership also. We have been paying the dues on that membership ever since he has had it.

He is the one that goes on the floor and does what business we have, and we pay all the dues on the exchange. No member of the firm ever goes on the floor of the exchange to trade. Now, how does that apply? I am a broker, and I have to pay this tax, and I am a member, and, of course, have to pay this tax if this bill holds the way it reads now. My employee is also a broker, but we pay his dues. He does not trade for himself; he trades for us. Is he to pay this tax also and also a tax because he is a member of an exchange, and yet he is trading for us and we are paying his dues?

The CHAIRMAN. Is he a member of your firm of brokers?

Mr. DIECKMAN. No; but he is employed under a salary.

Senator SMOOT. He would not be taxed under this bill. It says brokers shall pay \$100, and that goes to every person whose business it is to negotiate sales of stock.

Mr. DIECKMAN. He does it for our account.

Senator SMOOT. But you are the broker.

Mr. DIECKMAN. Your view is that he would not be taxed?

Senator SMOOT. Not under this bill. He is not the broker; you are the broker.

Senator NUGENT. He is simply your agent.

The CHAIRMAN. There is another tax. You have spoken of your membership dues. Do you object to that tax?

Mr. DIECKMAN. No; we are paying it in club dues now. I do not know that we will object to that so very much. Of course it is very excessive.

The CHAIRMAN. Now, I understand you are not specially objecting to the \$100 flat tax.

Mr. DIECKMAN. No; but we do object to the tax on memberships in the exchange in addition to being taxed as brokers.

The CHAIRMAN. Do you insist that that tax be stricken out altogether or do you suggest some substitute for it?

Mr. DIECKMAN. I think it should be stricken out absolutely so far as the smaller exchanges are concerned. Of course it does not apply to the New York Exchange. I suppose that 99 per cent of the business that is done in New York, whether in bonds or stocks, is done on the New York Stock Exchange, and nowhere else, except perhaps in some outside unlisted securities. They control all that business, and the volume is very large, as, of course, you gentlemen all know, and a \$150 tax in their case is absolutely nothing. They could afford to pay \$15,000, as compared with our little bagatelle amount figured in this schedule on our exchange membership.

The CHAIRMAN. I thought your original suggestion was that that rate of taxation should be re-formed so as to conform the tax to the amount of business done on the exchange.

Mr. DIECKMAN. Do you mean equally all around?

The CHAIRMAN. Yes; a graduating scale, starting at a very low tax where the amount of business is very small and going up to a very large tax where the amount of business is very large, as in the city of New York. But I understand you to say now that you think we ought to wipe it out everywhere except in New York.

Mr. DIECKMAN. That would be the easiest way for us to get out of the dilemma here. It is a tax on the business of the exchange. I do not know how that would figure out, but it would be a very small amount that we would have to pay as compared with what other exchanges would have to pay and would bring the whole thing in line where it is so totally out of line now as between New York, Boston, and Philadelphia and Cincinnati, St. Louis, and other places.

The CHAIRMAN. Your suggestion is that that tax should be placed upon a graduated scale; that the House scale is not equitable and just?

Mr. DIECKMAN. Yes; that is the way I feel about it. There is one more question. Your ruling as to whether a broker who pays a broker's tax under this bill and is a member of three or four exchanges like the stock exchange, cotton exchange, and so forth—

The CHAIRMAN. As I stated in the beginning here, we can not at this stage undertake to interpret the House bill or express any opinion about it. The House bill is not before us.

Mr. DIECKMAN. I do this merely to call your attention to it. I thank you, gentlemen, for your attention.

The CHAIRMAN. We are very much obliged to you.

(Mr. Dieckman subsequently submitted the following letter, which is here printed in full, as follows:)

ST. LOUIS STOCK EXCHANGE,
St. Louis, Mo., September 7, 1918.

Senator SIMMONS,
Chairman Senate Finance Committee.

DEAR SIR: We take the liberty of addressing you concerning a clause in the revenue bill which fixes a special license tax of \$100 upon brokers, and an additional \$150 if the broker is a member of a stock exchange.

We earnestly protest against the enactment of that clause in the bill and respectfully ask your aid to defeat same or secure a very material modification of its terms.

We protest against it because the bill is absolutely unjust to the smaller stock exchanges and their members in contradistinction with the larger exchanges, such as New York, Boston, and Philadelphia.

The proposed special license tax of \$100 upon brokers negotiating purchases or sales of stocks, bonds, and other securities and an additional tax of \$150 upon

such brokers who are members of an exchange would work a peculiar hardship upon brokers who are members of an exchange like the St. Louis Stock Exchange. This is a small exchange. At no time are there extensive transactions on the exchange as, for instance, on the New York or Boston Stock Exchanges, and at this time practically no transactions are being made on the St. Louis Stock Exchange. For instance, at a session of the St. Louis Stock Exchange on August 26, 1918, the total transactions were the sale of 9 shares of stock. On August 27 the sales were 20 shares. Occasionally there will not be a single transaction at a session of the exchange.

The commissions derived by a number of brokers who are members of the exchange will not warrant their retaining membership therein if, in addition to the payment of dues, they are compelled to pay a license of \$150 to the Government on account of their membership in the exchange.

The value of a membership in a stock exchange, or for that matter in any exchange, depends upon the amount of commissions that a broker can make through his membership. That is why a membership in the New York Exchange now sells at about \$60,000, while a membership in the St. Louis Stock Exchange could not be disposed of for \$1,000. To tax a broker for the privilege of doing business on the St. Louis Stock Exchange the same as a broker doing business on the New York Exchange would work a great inequality and would be closely akin to levying the same income tax upon an income of \$1,000 and \$100,000.

The vast details of accounting imposed upon brokers by the revenue act and regulations of the Internal-Revenue Department place additional expense and burdens on brokers, and such expense weighs most heavily upon brokers who are members of a small exchange like the St. Louis Stock Exchange, many of whom, by reason of small number of transactions made on the exchange, have a limited income from their membership.

Why brokers should be subject to a special tax for the privilege of doing business on an exchange is hard to comprehend. They are subject to all the taxes that corporations and individuals are subject to. They are subject to income tax and to excess-profits tax and during the periods of the sale of liberty bonds they gladly give not only themselves but all their employees and facilities to the sale of these bonds without any compensation from the Government.

The bill as it stands is prohibitive in its terms as applied to the smaller exchanges and their members, and we earnestly request your assistance with the committee in charge of the bill. Thanking you in advance for any assistance you may give us, we beg to remain,

Very respectfully,

ST. LOUIS STOCK EXCHANGE.
By J. H. DIECKMAN, *President*.
WM. L. ———,
Member of the Governing Board.

The total number of shares traded in on the St. Louis Stock Exchange for the entire year of 1917 was 128,478; market value, \$5,862,263.99. Bonds sold for the same period, \$1,056,240; market value, \$1,127,601.80; total value of bonds and stocks, \$6,989,865.79.

The CHAIRMAN. Mr. Fuller, I believe you said that you desired to be heard.

TOBACCO.

STATEMENT OF MR. THOMAS S. FULLER, COUNSEL FOR THE P. LORILLARD CO.

Mr. FULLER. There is just one feature of the tobacco tax that I wish to call your attention to, and that is the differential on the cigarettes, based on the price of cigarettes [reading]:

On cigarettes, if manufactured or imported to retail at 2 cents or more each, \$5.10 per 1,000.

The CHAIRMAN. You have the report in your hand.

Mr. FULLER. Yes; but it is the same print.

Senator THOMAS. Page 117 of the bill.

Senator SMOOT. Lines 15 and 16.

Mr. FULLER. It begins at line 11 and ends at line 16 [reading]:

On cigarettes made of tobacco or any substitute therefor, and weighing not more than 3 pounds per 1,000, if manufactured or imported to retail at less than 2 cents each, \$4.10 per 1,000—

Which is twice the present tax.

If manufactured or imported to retail at 2 cents or more each, \$5.10 per 1,000.

I am not speaking of the amount of the tax now, but of that differential. That works a very great injustice to a large amount of the cigarette industry in this way: There is already a differential on cigarettes that is not disclosed, because the only cigarettes that will sell for 2 cents or more apiece—if this tax goes in—will be cigarettes manufactured of Turkish tobacco—that is, I mean what is known as Turkish tobacco. Of course, no tobacco comes from Turkey now; but it comes from Greece and the Near East, and, that which was already in this country before the war.

Those are the only cigarettes that will sell for such a high price, and the cigarettes that are made out of home-grown tobacco and home-grown tobacco that is blended with Turkish tobacco all sell for a less price than that.

The pure Turkish cigarette is what I am speaking of. It pays already more than \$1 differential by reason of the import duty. These cigarettes weigh 3 pounds to the thousand. The tax on imported tobacco is 35 cents a pound. That is \$1.05, making no allowance whatever for the waste material, such as stems that are taken out.

So that the cigarettes are already on a \$1.05 differential, and when you take into consideration the enormous increase in the price of tobacco that is imported from the Near East it is a very, very precarious business at the present time. It is very difficult to get tobacco here under any circumstances. The insurance rates are enormous. The price of tobacco is itself almost prohibitive in the Near East. We could not get very much of it if it were not for tobacco that we had bought before the war.

That tobacco is shipped on small ships to ports in France, and then is shipped as return cargo in vessels that are going back. We try to ship on almost every ship that leaves Greece, but we have bad luck in losing about one in five or six ships.

If this differential is put on, it will not return anything to the Government of any consequence. The entire amount of Turkish cigarettes is about 2,000,000,000. The consumption in this country is about 2,000,000,000. So that that differential will amount in the total to \$2,000,000 a year if all of these cigarettes were consumed at that higher price. But if we put the price on the cigarettes so high, it will drive the consumer of that cigarette into smoking a cheaper cigarette, and they are fast going that way anyhow. I mean the increase in consumption of cigarettes is vastly greater in domestic-grown tobacco than it is in imported tobacco.

Senator SMOOT. Is not that a good thing?

Mr. FULLER. I am not arguing that it is not a good thing for this country. I do not think it makes much difference to the country so

far as the American farmer is concerned, because the entire amount of Turkish tobacco that goes into the pure Turkish cigarettes is but 6,000,000 pounds a year. When this country produces tobacco—8,000,000,000 pounds of it a year—it is an infinitesimal thing.

So that if there is no decrease in consumption whatever the outside amount that the Government could hope to raise would be \$2,000,000, with a real danger of destroying that business.

There are two concerns, particularly, in this country, subsidiaries of the P. Lorillard Co., one of which is known as S. Anargyros, a company in which we own all the stock. It would mean the wiping out of the business that has been built up and the enormous amount of money that has been spent in that building up; and I honestly believe that if it were put on the Government would lose money in the end, by reason of the company's not being able to make the money that it formerly did, and therefore not paying it in excess-profits taxes.

Senator JONES. On account of the increased tax has not the price of those Turkish cigarettes increased from 20 to 25 per cent?

Mr. FULLER. Oh, on account of the increase in taxation the price of all cigarettes has increased.

Senator JONES. But to the customer the price has increased from 20 to 25 per cent?

Mr. FULLER. I do not know the exact proportion of increase. The price increased so as to take up the increased tax on cigarettes and tobacco. That is a consumption tax.

Senator JONES. Has not the price increased sufficiently to absorb the tax heretofore levied in the increased tax?

Mr. FULLER. Yes, sir.

Senator DILLINGHAM. And more, too.

Mr. FULLER. It always does that.

Senator NUGENT. Has not the consumption of cigarettes increased very enormously, also, even at the higher price?

Mr. FULLER. The consumption of cigarettes has been increasing for a number of years, but the proportion of increase is less, considerably less this year than it was the year before, for the first six months. The proportionate increase in the consumption of cigarettes the year before was considerably greater than it was this year.

Senator THOMAS. I suppose there will be a prohibition crusade against tobacco pretty soon.

The CHAIRMAN. As I understand it, the general tax on cigarettes is increased in this bill from \$2.05 to \$4.10?

Mr. FULLER. That is it, sir.

The CHAIRMAN. That means cigarettes that are sold for less than 2 cents each a thousand?

Mr. FULLER. Yes, sir.

The CHAIRMAN. Then, if they are sold for more than 2 cents each, the tax, instead of being increased to \$4.10, is increased to \$5.10?

Mr. FULLER. That is it, sir.

The CHAIRMAN. Making the differential against cigarettes sold for more than 2 cents each \$1 per thousand.

Mr. FULLER. Yes, sir.

The CHAIRMAN. I understand you are saying that that class of cigarettes is made altogether out of Turkish tobacco?

Mr. FULLER. Yes, sir; that is true.

The CHAIRMAN. And that tobacco is imported, and pays an import duty of somewhere around \$1 a thousand?

Mr. FULLER. It pays an import duty on 1,000 cigarettes of something over a dollar. It would figure \$1.05, making no allowance for waste, such as stems, etc.

Senator JONES. Mr. Fuller, we are causing the people of the United States to reduce their consumption of sugar because we can not furnish the ships to bring it to this country from Java. Would it not be better to conserve the tonnage which is necessary to bring over this Turkish tobacco than to conserve the tonnage which is necessary to bring over the sugar?

Mr. FULLER. You could bring practically the entire amount of Turkish tobacco on one ship.

Senator JONES. I understand that, but 6,000,000 pounds, you say, of Turkish tobacco—

Mr. FULLER. No. We import altogether 20,000,000 pounds, and 6,000,000 pounds are used in this class of cigarettes.

Senator JONES. Would it not be better to bring in 20,000,000 pounds of sugar?

Mr. FULLER. This does not take any extra shipping. This tobacco that comes into this country only comes on ships as practically return cargo. The ship would have to come back in ballast if it did not take this tobacco.

Senator DILLINGHAM. It all comes from French ports?

Mr. FULLER. Practically so. There is some that comes in Greek ships that come over. They bring tobacco and a few other articles produced in Greece.

Senator JONES. We are considerably disturbed about obtaining pyrites and manganese from Spain. Would not these ships that bring tobacco from Greece be able to bring those metals from Spain?

Mr. FULLER. I have not the slightest knowledge of that. I am not in that business and would not essay a guess.

The CHAIRMAN. I understand there are 20,000,000 pounds that come over and but 6,000,000 pounds are used in these cigarettes that sell for over 2 cents?

Mr. FULLER. I could not say that comes over now, Senator. That would be incorrect. I mean that ordinarily, in normal times, there is about 20,000,000 pounds of Turkish tobacco imported, and that of that 20,000,000 pounds approximately 6,000,000 pounds go into the pure Turkish cigarettes; that is, unblended with any other tobacco.

The CHAIRMAN. What becomes of the balance?

Mr. FULLER. It is made up in blended cigarettes—cigarettes made of the domestic tobacco and the Turkish tobacco with it.

The CHAIRMAN. Do not most of the cigarettes made have a little Turkish tobacco in them?

Mr. FULLER. Yes, sir; most of them have a small amount of Turkish tobacco. I should think the lowest grades have may be 20 per cent.

The CHAIRMAN. That is for the purpose of flavor largely, is it not?

Mr. FULLER. Yes, sir.

The CHAIRMAN. They use a little of that Turkish tobacco just for the purpose of making the cigarettes more palatable, just as we use.

a little of this Egyptian cotton for the purpose of helping the textile qualities?

Mr. FULLER. Yes, sir; it adds a little flavor.

To guess at that mineral question, Senator Jones; to answer your question, it has occurred to me that I know nothing about the conditions existing between France and Spain—whether or not Spain could get that ore into France to meet these boats, you see. We have to deliver these tobaccos at ports.

Senator JONES. It is simply a question of tonnage.

Mr. FULLER. I know nothing about it, but I thought maybe that had something to do with it. These tobaccos do not come from Spanish ports.

Senator THOMAS. We have no convoy for ships between France and Spain.

Mr. FULLER. I know nothing about that. I know that ships go to Marseille and some other French ports.

Senator TOWNSEND. As a general proposition is that tax a liability upon the producer or a source of revenue to him?

Mr. FULLER. This particular tax will be in almost every instance no source of revenue to him, because it falls in a very awkward way. I do not wish to say anything about the amount of the tax. I did not come to speak on that.

Senator TOWNSEND. No; I imagined that.

Mr. FULLER. I do not wish to do that; that is all.

Senator TOWNSEND. I am interested, because I think you know about some of those things. There is a thing that has puzzled me a little bit.

Mr. FULLER. It is a consumer's tax and always has been.

Senator TOWNSEND. Quite so. We place a tax of 5 cents on tobacco under the present law. Take Piper Heidsick chewing tobacco, which I think is similar to other tobaccos. I am told that that is true. The retail price of a plug of Piper Heidsick before the war was 5 cents. There were 12 of those, I am told, in a pound. But immediately after the tax went into effect the price to the retailer went to 6 cents a plug, and now it is 7 cents a plug; that is, the consumer pays 24 cents additional for that tobacco, and the manufacturer pays 5 cents to the Government. Who gets the balance?

Mr. FULLER. I beg your pardon, sir. The manufacturer pays 13 cents a pound on that tobacco. Before the act of 1917 the manufacturer of that tobacco paid 8 cents a pound tax. Then the act of 1917 made that 13 cents a pound. Now this act makes that same tax 26 cents a pound.

You were in error in saying 5 cents. It was 13 cents. It was an increase of 5 cents. Let me point this out: In raising the price to the consumer the manufacturer, if there is any excess, has not taken that in profits. You must take into consideration the ingredients that go into tobacco. For instance, the cost of tobacco has increased anywhere from 200 to 300 per cent. Take leaf tobacco. You take tobacco that is being sold now on the opening markets in the South; it has averaged around 40 cents a pound. There has never been such a price for tobacco, certainly that I have ever seen in my experience, which has been something over 15 or 20 years.

Take all the other ingredients, like glycerine and licorice. Of course, we get very little licorice in this country any more. The

licorice root all comes from around the Persian Gulf, and it is tremendously costly to get anything of that kind. There are practically no importations any more, and that has put licorice up tremendously. Glycerine is very high. Practically everything is high, including labor, fuel—everything that goes into the manufacture of tobacco has increased perfectly enormously. Paper, for instance, that you wrap cigarettes in, is anywhere from 500 to 1,000 per cent higher.

Senator TOWNSEND. You go into the retail store—by the way, this increased price was put on the retail article before that act was signed by the President—selling for 6 cents, I mean; and the only excuse the retail merchant gave you was “the tax.” There had been an additional tax put upon it.

Mr. FULLER. If I recall correctly, the bill put a tax on the stuff on hand. That bill of 1917 put a tax on the stock on hand, known as a floor tax. So the goods that he sold after a certain date had to pay a tax. That is the reason for that, I think. The retailer was perfectly honest.

The CHAIRMAN. And contemporaneously with that increase in the tax occurred a very heavy increase in the price of leaf tobacco or raw material?

Mr. FULLER. Yes, sir.

The CHAIRMAN. And the increase in the manufacturer's price represents not only the increased tax but represents the increased cost of the raw material?

Mr. FULLER. Oh, yes, sir; if the tax remained the same as before the war, there would have to be an increase in the price, because of the cost of everything that goes into it—the cost of everything has increased.

Senator THOMAS. All of these various taxes are accumulated in the hands of the retailer and then passed on to the consumer?

Mr. FULLER. In all consumption taxes that is true, sir.

Senator THOMAS. This is a consumption tax.

Mr. FULLER. This is a consumption tax, of course, and it is assumed that the man who is going to consume the cigarettes and the tobacco is going to pay for it. The Government and the tobacco companies are in partnership in the tobacco business, and the Government is a preferred partner, because out of every pound sold the Government collects 26 cents before the manufacturer gets back even his capital investment. Out of every thousand cigarettes the Government takes off \$4.10 before the manufacturer even gets back the amount of the investment. I am not speaking of the amount of the tax. I am speaking simply of this differential, which I do not believe will return \$1 to the Government.

The CHAIRMAN. You are not objecting to the tax on cigarettes; you are objecting to making a differential against a small lot of cigarettes that are made out of Turkish tobacco?

Mr. FULLER. Yes, sir; it will practically wipe out that business without any attendant benefit to the Government whatsoever.

I thank you very much, sir.

The CHAIRMAN. Mr. W. L. Dawson will be next heard. What business do you represent, Mr. Dawson?

STATEMENT OF MR. W. L. DAWSON, CORPUS CHRISTI, TEX.

Mr. DAWSON. I am representing the farming and stock-raising interests in the southwestern part of my State, Texas, and I desire to address the committee—

The CHAIRMAN. How long will it take you?

Mr. DAWSON. About 15 or 20 minutes, I think, will be sufficient.

The CHAIRMAN. Will you be satisfied with 20 minutes and not ask for an extension?

Mr. DAWSON. I will do my best; and at the end of that time, if the committee desires, I will suspend, regardless of whether I have finished or not.

Gentlemen, the feature of the bill which is applicable to the issue that I wish to call the committee's attention to is peculiarly applicable to my section of the State, which is a part of the drought-stricken region of the United States, and the conditions that I wish to call your attention to are those with which you gentlemen can not possibly be familiar enough to be able to measure the effect unless you are apprised of those peculiar conditions existing there.

These conditions apply equally to the farmer who is tilling the soil and producing foodstuffs and cotton as it does to the man who is utilizing his lands in the production of cattle, sheep, goats, and so on; but, of course, the cattle is the principal industry.

In that section of the State we have our cycles of difficulties, and unfortunately we have in my particular section just gone through a cycle which has been the worst in the history of that country.

The farmers in that section of the State have made nothing for three years. They have been carrying the burden of their losses through those three years indirectly or directly, and most of them have been carrying it indirectly, because it has been necessary that they be financed by somebody because they were not financially able to sustain the losses and carry the burdens and make any profit.

Therefore I want to give you some concrete illustrations that I think by investigation will verify every bit of it.

In order that you may understand the peculiar condition of which I speak, I wish to say that in my section of the State within the last 6 or 8 years agriculture—that is, farming—was practically unknown. The land was all in vast ranches. Some 8 or 10 years ago the ranchmen began to cut up their ranches and allow them to be sold out to actual settlers, to farmers. Unlike a great many sections of the country, those farms had not been settled up in 40 and 80 acre farms, but a very large percentage, amounting easily to 75 or 80 per cent of the tillable land which is in actual cultivation to-day, is cultivated by men who have bought and are cultivating their one-half section or 360 acres up to, in many instances, five and six thousand acre farms.

You can readily see that as to the burden of carrying a farm of that kind the expense that that man has to incur in order to carry out that development is very great.

Men have gone through a period, as I say, of three years now, and they have received nothing in return except debts. They have enor-

mous debts, comparatively speaking, piled upon their shoulders, and in each instance almost the farmer has been financed for the last two years, and in fact in a majority of instances, all the way through these three years by some one. And I want to say this, that in very few instances has it been the local bank, because the banks have not been in condition for the last few years to finance the farmers. They have placed chattel mortgages on their crops that they were going to produce.

This year for the first time we are making some crops in that section of the State, and I can safely say that that community as a whole, while we have what they call a "bumper crop," in some sections this year will not pay off the debts that have been incurred in the last three years.

Now, you take a farmer who produces this year \$10,000. I can assure you, gentlemen, that an investigation will verify the statement that the \$10,000 crops produced by the farmers in southwest Texas—and I think that would apply in many other sections—will not discharge their financial indebtedness, for it is safe to say that this indebtedness will average \$10,000.

The bill as introduced in the House provides a \$2,000 deduction for him individually. Then the United States is calculating to collect \$965 due by him, and his expenses for this year will, conservatively speaking, run him over \$3,000. His overhead indebtedness will run from \$6,000 to \$8,000, with his creditors holding a mortgage on his crops. Those crops, in the majority of instances, are largely harvested to-day, and most of them have been sold and delivered. The farmer has done only what he could do under the law. He has delivered his crop over to his creditors. The creditors, be they whom they may, are receiving money that they have advanced this man. At the end of the year he will not even have a dollar left. Yet he owes the Government \$965 in June. Where is the farmer going to get the \$965 to pay the Government? That is an overhead debt that he has incurred in actual production. There is created an emergency that leaves him in just that condition—

Senator SMOOT. There is no provision in this bill that a farmer whose gross return is \$10,000 will be taxed \$965.

Mr. DAWSON. I beg your pardon. If I understand the bill correctly—

Senator SMOOT. Then you do not understand the bill correctly, and if you are arguing to that effect there is no such thing in this bill.

Mr. DAWSON. Is there a distinction made between the farmer and any other individual?

Senator SMOOT. None whatever. He has a perfect right to take off whatever cost there has been in producing that \$10,000 gross return.

Mr. DAWSON. All right, then; we will take off the \$3,000 that he is allowed there. You have got, then, \$7,000.

Senator SMOOT. He has an exemption of \$2,000.

The CHAIRMAN. You do not mean to say that a farmer who makes \$10,000 made it at a cost of \$3,000?

Mr. DAWSON. No, sir. I set it at the minimum cost. I put it at the minimum amount.

Senator SMOOT. What would be the cost?

Mr. DAWSON. I think that from \$3,000 to \$3,500 will be the average of a crop this year. You must understand, gentlemen, that you are dealing with a condition which is different in every way. You take the cotton farmer. This year he has spent three or four thousand dollars. It is nothing for him to be receiving a \$10,000 return for his crop.

Senator SMOOT. That is true.

The CHAIRMAN. Mr. Dawson, I do not understand that. The farmer that is getting 30 cents for his cotton this year will make some money, but if you consider the price that he has got to pay for fertilizer and the price that he has got to pay for labor, he is not going to have any such profits as you indicate. Not in my country. I do not know how it is in your country.

Mr. DAWSON. I see the point, Mr. Chairman—

The CHAIRMAN. You have got to take out the expense of the fertilizer and the expense of his labor and the expense of his farming implements, or a reasonable allowance for his farming implements; and you have got to take out various and sundry other expenses. The interest he pays on his debt, and all those things, have got to be deducted—

Mr. DAWSON. If you will pardon me just a moment. Your suggestion, Mr. Chairman, reiterates and emphasizes exactly what I contend, that you are dealing with a condition now that you gentlemen are not familiar with. I think you will admit that one of the principal costs in your section of the country would be the fertilizer.

The CHAIRMAN. That is a large thing, of course.

Mr. DAWSON. We have no such cost in our part of the country.

Senator THOMAS. What difference does it make what the items are which constitute the cost? Whatever they are, they are deducted, under this bill, from the amounts received.

Mr. DAWSON. That is correct.

Senator SMOOT. If you do not have to use fertilizer, you are that much better off than the fellow that does.

Senator JONES. The point which Mr. Dawson is seeking to make, as I gather it, is one of very great importance not only in that section of the country but in other sections of the country as well. Stated broadly, I take it to be this: Here is a farmer who for two or three years has been losing money—

Mr. DAWSON. Accumulating debts.

Senator JONES. He has been accumulating debts. He has gone to the expense of trying to raise a crop which did not materialize. This year he hopes to make a profit. That profit, under the existing law and the proposed bill, would be taxed as income of this year without reference to his losses in previous years.

Mr. DAWSON. Yes, sir.

Senator JONES. The point which you make exists not only with reference to the farmers in that section, but in other sections, particularly the live-stock men.

Mr. DAWSON. I was coming to that.

Senator JONES. Some years they make large profits. Other years they make losses.

Mr. DAWSON. Yes, sir.

Senator JONES. And under the English system of income taxes there is a provision for equalizing the business over a period of about three years.

Mr. DAWSON. That is what I was trying to come to, if the Senators would kindly permit me.

Senator SMOOT. The same thing applies to fruit growers of my own State. We have had frosts for three years there. They have not had enough out of the fruit to pay for the boxes they need. I will not interrupt you any further, but let me say this: This has been threshed over, time and time again, with the committee. I do not want to take any more of your time and I will be glad to hear what you say about it.

Mr. DAWSON. If the committee will kindly pardon me, I am trying to put before you a condition and show you what the result is going to be under the proposed bill. Then I will leave it up to you gentlemen.

I want to say this, that I am dealing with a question that affects an enormous production territory from the standpoint of foodstuffs and cotton. I will say that it affects fully between 20 and 25 per cent of the feed-cattle production. It is a matter worthy of your consideration, and if there is any opportunity to meet it I hope it may be met so as not to absolutely destroy the productiveness of that section.

The man is in debt. What he has got is security for that debt. I started in with the little \$10,000 farmer, because that is the simplest problem. As I stated, when you get up to the \$50,000 and \$100,000 class, he is in every way in the same difficulty as the \$10,000 farmer. You will destroy that man. Why? Because his creditors are taking his money. What is he going to do when the time comes to pay the Government? He has not got a dollar with which to pay it.

Senator SMOOT. The creditors are not going to take it away.

Mr. DAWSON. They have already taken it, if you please, in a great many instances. I am speaking of instances in which the crop has already been delivered to the creditors; the debt is discharged—

Senator SMOOT. Then they can borrow money.

Mr. DAWSON. The bank is not going to loan them money, for the simple reason that the same condition will come on to them next year. The bank is not going to loan money unless it has some chance of getting it back—at least no bank that I know of or have ever had any dealings with.

Let me make this application to the cattlemen—

The CHAIRMAN. Before you leave the farmer: I understand you to say that he has accumulated certain debts due to these lean years.

Mr. DAWSON. Yes, sir.

The CHAIRMAN. And all those debts are consolidated and made this year a mortgage upon his crop?

Mr. DAWSON. Yes, sir, because it is a renewal debt each year. The man who is trying to back him wants to get this year what he sunk last year, and he had confidence enough in the country and in the man he was dealing with to carry him. That man has honestly entered into the contract and is staying there and working it out and doing his best to pay off the debt. You take the \$50,000 and \$75,000 man who is farming on a larger scale. If he breaks even

this year he is lucky. What is he going to do when it comes time to pay the Government? Go to jail, or must he go into the courts of the State and enjoin his creditors from collecting the debt, on the ground that the Government wants and must have a part of that debt? If he does not go into the courts, the creditor is clearly going to take his property.

Senator THOMAS. Can he go into the courts and do that?

Mr. DAWSON. I do not think he can, to be frank with you.

What will be the result in June when that man is called upon to pay the federal officer his tax, and he has not got it? Is he going to go to jail?

The CHAIRMAN. Were those past due debts secured only by mortgage on the crop, or mortgage on the crop and the land?

Mr. DAWSON. In a great many instances he is a tenant farmer and does not even own his land. I happen to have in mind one particular man that I have been in touch with and in constant touch with throughout the dry period, and I have talked with him a number of times. When he started in this year his indebtedness was \$16,000, and he does not own a foot of land at all. He is a tenant farmer, but he is a good farmer, and his landlord assisted him in his farming venture. That man is going to make between \$20,000 and \$25,000 this year. That will not cover his indebtedness this year, and he has already mortgaged to secure—

Senator SMOOT. Why won't he cover it? I cannot see, for the life of me, what there is to prevent him—

Mr. DAWSON. If the Senator had listened to what I said—I said he started in this year with an indebtedness of \$16,000 hanging over him—

Senator SMOOT. The same thing happens in manufacturing institutions. But what I want to know is what suggestion you make.

Mr. DAWSON. I simply wish to suggest conditions to you, gentlemen. I am not legislating.

Senator SMOOT. You want them exempted?

Mr. DAWSON. I want some allowance made for the debts these men have incurred in trying to produce for the United States, in order that they may pay those debts before they have to pay it to the Government, and destroy the producing agency in that section of the State.

Senator SMOOT. That happens all over the United States.

Senator THOMAS. What you want is some allowance for debts they have incurred in previous years?

Mr. DAWSON. Yes, sir.

As to the cattlemen, I want you to bear with me just a moment for this side of it: The cowman has been carrying his cattle in like manner, and that is a big feature. The average cowman does not own all of his cattle, does not have them paid for, you understand. I think you can get that from various sections of the country. But the cowman who owns his land buys a bunch of cattle. He pays \$75,000 or \$100,000, and he is paying interest on that money. The growth of those cattle will make money for him on the range he has got. In the past few years he has not only lost money in deaths from the drought, but has been paying expenses in shipping those cattle and getting what he can for them. If he sells those cattle for enough

to pay his debts, considering the growth and age of the cattle, he is a lucky man. Yet, the debt was incurred three years ago that he paid for those cattle. His operating expenses will not be more than \$15,000 or \$20,000. Yet he owes for every dollar of those cattle. It is a pre-existing debt. They are under mortgage.

I am speaking now of a condition that I am thoroughly familiar with as to its existence. The Live Stock National Bank of Chicago carries millions of dollars in just that kind of loans. Mr. Trailler, the president of that institution, at a conference in Houston with some cattlemen at which I happened to be present, took under consideration the question of saving those cattle, and the question of what they were going to do came up. Mr. Trailler said, "We will never make a wet weather loan. We always make a loan that we can carry through dry weather. If you know of any pastures, move those cattle to them and draw on us for your money to move your cattle and take care of them."

The cattle are under mortgage, you understand. They have got a \$100,000 increase this year for their cattle with only a \$20,000 or \$25,000 expenses account that they will get credit for. Yet they owe that whole amount.

What is the ranchman going to do? Is he going to pay the Government a tax on that \$75,000 or \$80,000 income for this year?

I am trying to present facts to you; I am trying to present conditions to you, and they are worthy of your consideration, because this is dealing with one of the biggest productive features of our Government to-day.

So far as the farmer is concerned, I will say this. It has come under my observation and I have had opportunity to see, that there are in that section thousands of acres yet undeveloped that the ranchman is willing to have put on the market. But when you get to talking to a farmer about putting the land in cultivation, he says, "I can pay you a cash payment." You put it to him on easy terms. "I can clear my land and put it under cultivation, but I have got to pay for my land out of the production from it. With that tax on it I can not do it, and I will not sink what I have got. It means that the original vendor or the Government gets my land and I sink what I have in it."

The CHAIRMAN. You say the man owed \$16,000 when he started in?

Mr. DAWSON. Yes, sir.

The CHAIRMAN. And this year, on account of the higher prices that he has been able to receive, he has paid off that \$16,000 in one year?

Mr. DAWSON. Yes, sir.

The CHAIRMAN. Now, you say if he paid that off he owes, instead of \$16,000, \$900 for taxes. Then he is \$15,000 better off than he was a year before.

Mr. DAWSON. I beg your pardon. I did not say he owed \$900 on a \$25,000 income—

The CHAIRMAN. If he had \$16,000 worth of debts, he deducts the interest on that \$16,000. Then he has \$8,000 worth of expenses to be subtracted; so that you would have him down to a net income not of \$20,000, but not over \$10,000.

Mr. DAWSON. But if that is all gone, how can he pay? Suppose he only owes the Government \$500?

Senator SMOOT. He would not owe the Government \$500 under any bill that we have under consideration, if those are the facts as stated by you.

Senator JONES. Oh, yes; I am sure he would.

The CHAIRMAN. If he had accumulated an indebtedness of \$16,000, and now, by reason of the higher prices during this year he has paid off the \$16,000, he simply owes a tax account, and the tax account is all he owes as against that \$16,000. His condition has been greatly improved.

Mr. DAWSON. His condition has been greatly improved, but he has not paid his tax to the Government. And how he is going to pay it is the question.

Senator SMOOT. If he can not borrow money to pay what little taxes he owes, how on earth is he going to borrow money to go on with the business? He has got to have a credit somewhere.

Mr. DAWSON. Pardon me for suggesting this, but I wish you would please get away from the little \$16,000 man. I started off with the small one to try to illustrate.

The CHAIRMAN. I want to make this suggestion to you: I do not know how far the Government lien upon the property for taxes extends. I do not know whether it would extend to cover that crop in the hands of his creditors or not. But if it did not cover that, and he has disposed of all of his property, he has turned over all his property and got nothing, how is the Government going to get the money?

Mr. DAWSON. The bill says that he will pay a fine of a thousand dollars if he does not pay it.

Senator THOMAS. Suppose he does not pay it?

Mr. DAWSON. If he does not pay it, he goes to jail.

Senator THOMAS. That is an assumption.

Mr. DAWSON. Do you know of any law which provides that you shall be turned loose if you do not pay your fine?

Senator THOMAS. I know where a fine is placed—not in the shape of a tax—

Mr. DAWSON. There is a penalty provided for failure to pay. It is a criminal offense.

Senator THOMAS. Oh, no. It is a default.

Mr. DAWSON. A failure to pay a tax is a default, but the bill itself makes it a penal offense with a fine of \$1,000 if he does not pay. How can he pay the fine if he can not pay the tax? What is the result if he is fined by the court and does not pay the fine?

Senator THOMAS. There is a penalty for the default. I do not know that you can find any instance in the history of taxation where a penalty for default has been followed by proceedings which deprive the defaulter of his liberty. I do not think so. I may be mistaken. I do not pretend to know it all.

Mr. DAWSON. What about the man that has \$100,000 of indebtedness, and we will say, for the sake of round numbers, that he produces \$100,000? If you gentlemen will please get away from the little man just for a moment—

Senator THOMAS. Let me explain. I distinguish between the man who defaults because he has not anything to meet his tax with, and the defaulter who deliberately tries to defraud the Government

by concealing or otherwise evading his tax. That is an offense, of course, for which there ought to be appropriate punishment. My remarks have reference to the man who does not pay and who defaults because he has nothing with which to pay.

Mr. DAWSON. The bill makes a distinction there, you say?

The CHAIRMAN. Certainly if a man's creditors take all his property away from him and by reason of that fact he has nothing with which to pay, has no income to pay with, then of course he can not be held by any court as a criminal offender. He may default in the payment of his taxes and a fine may be imposed upon him which would be taxed against his property; but no court in this world would fine a man for a thing of that sort.

Mr. DAWSON. Conceding that your judgment of what the courts are going to do is correct, then—

Senator SMOOT. Getting back to the \$100,000 man, the man owing \$100,000—

Mr. DAWSON. Yes, sir; and his income is \$100,000.

Senator SMOOT. His income is \$100,000?

Mr. DAWSON. Yes, sir. There are lots of them that will just about break even this year.

Senator SMOOT. His investment was \$100,000 and his income is \$100,000?

Mr. DAWSON. I am not talking about his investment. I am talking about his debts.

Senator SMOOT. He invested his debts.

Mr. DAWSON. His debts were a part of his investment. Suppose he owned the land and still owed \$100,000 besides, and he produces \$100,000—

Senator SMOOT. Then he would be ahead exactly the amount over and above what is provided under this bill. He would be that much better off than he was when he started.

Mr. DAWSON. That is true, certainly.

Senator SMOOT. It seems to me he is a very fortunate man.

Mr. DAWSON. He is in that he is able to produce that—if he could go on and produce it next year.

Senator SMOOT. I can not understand your theory at all. If a man in the past has been able to secure credit, and his standing in the community is such that he can go and borrow \$100,000, I have not any doubt but what the same man can borrow again.

Mr. DAWSON. The Senator is confusing the \$100,000 man with the little man again. The \$100,000 man, I do not say borrowed it. It was probably in all cases secured by liens on his land, the vendor's land. He did not borrow it. The open-handed Government can make it out of him because he has got land to make it out of; but when they sell his land to pay the Government \$25,000 or \$30,000 and his crops have already been taken for his creditors, then he still is liable to the Government, and the Government can make it out of him, but he will not have his land to make it on next year.

The CHAIRMAN. Mr. Dawson, I think the committee generally understand your position very clearly and is obliged to you for presenting it, and the committee will give it consideration. Some of the Senators say they desire to attend to some other matters, now. Your

time has been exceeded. If there is any other phase of it you wish to present—

Mr. DAWSON. There is another phase. I wish you would bear in mind that, as Mr. Kitchin stated on the floor in his address to the House yesterday afternoon, he said it was perfectly right that the corporate interests of the country should be allowed to pay 10 per cent profit on their investment for this year as against 6 per cent they were allowed heretofore.

If corporations are allowed a profit, conceding that they are essentials, such as the banks and other interests that handle this stuff, the cattlemen, producers, then I want to know where the essentiality of the cattleman, who is largely the corporation, is going to come in if you cut off the producer? If the producer that I spoke of, the \$100,000 man, who owes the \$100,000 and pays his debt, and then the Government comes in for \$25,000 or \$30,000, he has got his land and the Government can make it out of that; but then you have ended his production because of it.

You have got a condition there where he is not being allowed his 8 per cent because of the fact that he has gone over a period of six years—

Senator JONES. I would like to state for the record at this point, Mr. Chairman, that the point raised by Mr. Dawson is a real problem and it is one which deserves the most earnest consideration of this committee.

The English law meets the situation by imposing an income tax with reference to a period of three years, as I understand it; and where a man makes losses in one year the amount of the income tax for the good year is taken into consideration with the losses of the bad year, and equalized in a measure.

Mr. DAWSON. That would meet the emergency here.

Senator JONES. This is a real problem. I sincerely trust that the committee will give it very serious consideration before this bill is framed.

Mr. DAWSON. I thank you, sir.

The CHAIRMAN. I wish to say that the committee will, of course, give Mr. Dawson's suggestions serious consideration, as we propose to give the suggestions of any gentleman that comes before us. We are glad to hear Mr. Dawson. He presents a rather exceptional case. We will consider it.

I want to announce now, however, so that there may be no misunderstanding about it hereafter, that we will try at our next meetings to fix a limit for all gentlemen who appear before the committee, and unless a gentleman is interrupted too much in his time and unless the committee thinks it will be necessary for him to have more time, we will not extend the time.

I am not speaking particularly of you or anybody else, Mr. Dawson, but I am simply saying that we will have to have such a rule.

To-day we have not had many gentlemen here who desired to be heard, and therefore we could be a little liberal. Probably next week we will have a great many people who are anxious to be heard, and in order that all may be given an opportunity to be heard, we will have to impose some limitation.

You and Mr. Marsh were allowed a wide latitude because we did not have many people who insisted on being heard, and we therefore had the time to give to you.

Mr. Dawson. May I say this for the people of my section, that if these debts can be allowed to be taken care of I doubt not that every farmer in my section and every cattle raiser in my section will be willing for the Government to fix a tax taking every dollar of profit that they have until the termination of the war, and obligate themselves to cultivate every acre of their soil and utilize every acre of their pasturage in the production of feed cattle and in the production of cotton and foodstuffs—

The CHAIRMAN. No one will question the magnificent spirit of the farmer, Mr. Dawson.

Unless there is objection to the change, we will adjourn at this time to meet at 10.30 o'clock on Monday, instead of 10 o'clock.

(Whereupon, at 12.30 o'clock p. m., the committee adjourned to meet at 10.30 o'clock a. m., on Monday, September 9, 1918.)

TO PROVIDE REVENUE FOR WAR PURPOSES.

MONDAY, SEPTEMBER 9, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10.30 o'clock a. m. in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present: Senators Simmons (chairman), Williams, Smith, Thomas, Gore, Jones, Nugent, Penrose, Lodge, McCumber, Smoot, Townsend, and Dillingham.

The committee resumed the consideration of the bill (H. R. 12863) "to provide revenue, and for other purposes."

The CHAIRMAN. Gentlemen of the committee, we have a majority here, and the committee is ready to proceed with hearings.

CIGARETTES.

STATEMENT OF MR. WILLIAM M. MARTIN.

The CHAIRMAN. How much time will you need?

Mr. MARTIN. I think I ought to get through in 10 minutes.

The CHAIRMAN. We will give you 10 minutes, if that is enough.

Mr. MARTIN. Thank you, sir.

I am from Petersburg, Va. I am not a speaker, but the matter that I want to refer to is a provision in this revenue bill on page 62.

I would say that in Petersburg we have a bonded manufacturing warehouse, class 6, for the manufacture of cigarettes. It is the largest industry we have there, employing probably about 3,000 to 4,000 in a town of about 30,000 people. I should say that certainly one-tenth of our population was engaged actively in this business.

Senator NUGENT. What section of the bill are you discussing?

Mr. MARTIN. Section 1002.

Senator THOMAS. You said page 62.

Senator JONES. He is reading from another print.

Mr. MARTIN. It is section 1002.

The CHAIRMAN. You have the report, have you not?

Mr. MARTIN. Yes, sir.

Senator DILLINGHAM. It is page 144 of the bill.

Mr. MARTIN. The British-American Tobacco Co., as I say, manufactures cigarettes under a law that was passed under President Cleveland's administration, establishing this class of warehouse. Under a provision of that law all articles imported for use in the

manufacture of cigarettes are shipped in in bond and are not subject to any import tax. It comes in in bond, is shipped from the port to the factory in bond; the factory itself is in bond—everything that goes in it is under the control of Government representatives.

These cigarettes are manufactured from Virginia and North Carolina and South Carolina tobaccos mostly. They are manufactured in bond. They are shipped in carload lots, most of it to China; some of it to the British army; but while it is in the cars it is in bond, under Government seal, and it stays in bond until it goes out of the country.

The object, as I understand it, of establishing these factories was to exempt the manufacturer from the internal-revenue tax. This matter was, of course, up before the Ways and Means Committee. It was only called to my attention last week. The Ways and Means Committee of the House in the consideration of this matter seem not to have considered at all the export phase of the tax. So that the point I want to make is with reference to this (reading):

That on and after January first, nineteen hundred and nineteen, there shall be levied, collected, and paid annually, in lieu of the taxes imposed by section four hundred and eight of the revenue act of nineteen hundred and sixteen, the following special taxes, the amount of such taxes to be computed on the basis of sales for the preceding year ending June thirtieth.

I have here a letter from Mr. Thurman, the Acting Secretary and Solicitor of the Department of Commerce, and if you do not object I would be glad to read this—certainly a part of it.

Senator SMOOT. Why not insert it in the record as a part of your remarks?

Mr. MARTIN. I shall just read one or two sentences. I think it will probably save a little time (reading):

I find that in connection with section 600 of the revenue act of October 3, 1917, the Assistant Secretary of the Treasury has approved a ruling of the Commissioner of Internal Revenue which holds that the tax imposed by said section upon the sale of automobiles and other enumerated articles is not applicable to such articles when normally exported. It seems to me that the two taxes, while of a somewhat different nature, are both in essence taxes on sales of certain products and as such subject to the same reasoning as respects the distinction between export and domestic sales. Unfortunately, however, the Commissioner of Internal Revenue has not yet ruled that the tax provided for in section 408 of the act of 1916 should be computed on the basis of domestic sales only. For this reason I think it desirable to bring to the attention of your committee the effect of this tax provision as at present applied, with the thought that perhaps it will be found advisable to insert a clause in the present bill specifically exempting export sales from the imposition of the tax in question.

That is the view of the Department of Commerce.

The CHAIRMAN. You mean if your tobacco is exported, then it should not be subject to the internal-revenue tax imposed in the bill?

Mr. MARTIN. Certainly; that is exactly what I am getting at.

Senator SMOOT. That has been generally the case if the tobacco had been imported into the country, but it has never been—

Mr. MARTIN. I beg your pardon, sir. If you will refer to the decisions—

Senator SMOOT. I am speaking of the tobacco. I am not speaking of the bill itself passed in 1917.

We have a general provision that wherever the articles are imported they can be manufactured and exported without paying the

duty; but I do not remember any such legislation as you are asking for now in relation to the manufacture of domestic tobacco to be exported being relieved from tax.

Mr. MARTIN. I will go back a little. As you of course understand, the internal-revenue tax was established practically during and following the Civil War. Among articles that were taxed was tobacco. Of course, we have got a stiff internal-revenue tax on that, but the tax we have had for tobacco exported was 25 cents on each package of tobacco, which did not make any difference as to how many pounds it was.

The United States Supreme Court, through Mr. Justice Bradley, decided that that was not a tax; it was simply a means of identifying the article so as to exempt it from the internal-revenue tax. Do you see the point?

Senator SMOOT. We can look that up without you taking your time.

The CHAIRMAN. My understanding is that no tax is imposed on tobacco or anything else that is exported.

Mr. MARTIN. If I may just call your attention to the former bill, which was effective the 1st of January, 1917, it imposed a tax of 3 cents. This tax doubles it. That is, per 10,000 cigarettes.

That tax has never been questioned. It was simply a small matter; it did not amount to more than 25,000 to this company. Now it is proposed to double it.

The point I am getting at is this: I was told by a director of the American Tobacco Co. who talked to me about this the other day that they will not do anything that will prevent the Government from getting all the money it needs. He spoke about the increased tax that that company and its subsidiary companies will pay—a million dollars at least—this next year. We are not speaking about that. What we object to, and what I want to call your attention to, is the precedent that is being established of taxing sales of cigarettes for export. It is a reversal of the policy of the Government as established during the Civil War and subsequent to the Civil War. The tax last year amounted to about \$25,000.

In talking with one of the directors of the company he said they never had any hearing before the Ways and Means Committee and they were sure this thing was stuck in in both cases through inadvertence; that it was not the intention to tax sales of tobacco for export. The bill clearly says so. It does not say "for export," but it says "computed on the basis of the sales for the preceding year ending June 30." It does not say "domestic sales."

The CHAIRMAN. That is the point you are making?

Mr. MARTIN. That is all.

The CHAIRMAN. You think it ought to be reduced to the extent of the sales that go into export?

Mr. MARTIN. That is all. It is just simply a part of the business.

I would like to say one other thing so as to justify my appearing here.

Some time ago the Railroad Administration fixed a rate on this same tobacco, most of which, as I say, goes to China—and incidentally I might say that I have a report here showing that the competition that Japan is putting up against this company is simply enormous,

and the increase in Japanese business in China is rapidly superseding this company's business. But what I wanted to say is this: It is not the amount of money involved that I am driving at; that is a small part of it; but if this precedent is established it will mean the reversal of the Government's policy heretofore. Another thing is that possibly some question of constitutionality is involved in regard to Congress having authority to impose a tax on articles exported from a State. I am not emphasizing that, nor the money end of it; but I will say that the last experience we had with the Railroad Administration is nothing short of appalling. I will give you a synopsis of it.

The rate on a carload of cigarettes from Petersburg to the Pacific coast points was \$400—a dollar a hundred—40,000 pounds to a carload. This company ships exclusively in carloads. Without any hearing or without any investigation that we can find out, the Railroad Administration shoved the rate up to \$1,200 a car. Mr. Duke said he would move his business out of the country; he would not stand for it.

I took the matter up with Judge Chambers and Judge Prouty. They cut the rate from \$1,200 to \$600. That is the rate effective since July 1.

So far as this taxation of sales of tobacco for export is concerned, that has not been the policy heretofore of the Government. The only case they did that is when they stuck this 25 cent tax on as a means of identifying the tobacco. The constitutional view is to exempt that.

I will say, further—and I do not want to be misunderstood—that I am interested in it because my town is interested in it, and I believe this thing is an inconsistent attitude, at least a reversal; I will not say inconsistent. It is absolutely a reversal of the policy heretofore established.

This company has a branch in Richmond, one in Petersburg, and one in Norfolk. They employ about seven or eight thousand people. I am not asking relief because of that fact. I am not asking it on the basis that the company will save a little money by it. I am not asking it on the ground that we want to keep our people employed. I want it on bigger ground than that. I say if the policy of this Government is announced in this bill and the Government persists in taxing exports, when the exclusive business of that company is export—this company does not sell a dollar's worth of cigarettes in the United States—they can get cheaper labor in China; their market is in China, and they can move to China. Mr. Duke, president of the company, has advocated it. He has only been held back by his directors, most of whom are Virginians and North Carolinians, who want him to keep his business in this country. This company would lose at least a million dollars in the next 12 months.

Senator Smoot. I want to say this, Mr. Martin, that this is not an export tax. This is a tax upon sales made in the United States. I think there is quite a difference when you come to a question of law between the imposition of an export tax which is against the Constitution and a tax upon sales, whether it be made to a local concern or whether it be made to a foreign concern. It is a question of a sale tax. It is worthy of consideration, though.

The CHAIRMAN. Yes; I think the committee fully understands the point.

Mr. MARTIN. If every dollar's worth of its business is done abroad, they bring it back and spend it in this country, of course.

Senator SMOOT. I am aware of that.

Mr. MARTIN. Of course you admit that it is simply a matter of the difference between six and half a dozen, if you put in there "sales for domestic consumption." But the point is that it might come up as to whether that sale was effected in this country—

The CHAIRMAN. I think the committee fully understands your point and appreciates it. We will give it close consideration. But I do want to say in connection with your suggestion that Mr. Duke is threatening to move over to China—

Mr. MARTIN. They have a factory there now.

The CHAIRMAN. Some tobacco manufacturers of this country moved over to Japan, and within a very short time after they got over there and installed their plants, Japan commanded them.

Mr. MARTIN. They practically forced them to sell, but they sold at a good price. And, by the way, it is those factories there that are producing the competition that this country is up against now.

SENATOR THOMAS. Then Mr. Duke and his people are indirectly responsible for it.

Mr. MARTIN. No, sir; they are not indirectly responsible for it. They had no choice.

SENATOR NUGENT. Did your company recently make an appeal to the Government to protect them in some way in their tobacco trade with China, which amounts to thirty millions a year?

Mr. MARTIN. Several matters have come up in connection with it—

SENATOR NUGENT. I saw a statement in the newspapers some time since to the effect that your company had appealed to the Government to protect them in the tobacco trade in China, which, according to that newspaper statement, amounted to something like \$30,000,000 a year. Is that correct?

Mr. MARTIN. I should think it would be around about that.

THE CHAIRMAN. It was reported at that time, I think, that the Japanese had gotten a foothold in China so far as the tobacco trade was concerned, and they were agitating with a view to getting China to adopt the same policy that Japan had adopted; that is, to take over the tobacco trade and commandeer private factories located there.

SENATOR NUGENT. I have read something about the matter, but my recollection is indistinct.

Mr. MARTIN. Could I just file this letter?

THE CHAIRMAN. Yes.

(The letter referred to is here printed in full, as follows:)

SEPTEMBER 9, 1918.

MY DEAR SENATOR Section 408 of the revenue act of 1916 provides for special taxes to be paid by manufacturers of tobacco and certain tobacco products, which taxes are to be computed on the basis of the amount of sales of such products by the manufacturer during the preceding fiscal year. Article I of the Constitution provides that "no tax or duty shall be laid on articles exported from any State." As you probably know, our exports of tobacco and tobacco products are very substantial and if the taxes referred to are to be computed on export sales as well as domestic, it may, if increased as proposed in the present revenue bill, prove quite a deterring factor in our export trade.

I find that in connection with section 600 of the revenue act of October 3, 1917, the Assistant Secretary of the Treasury has approved a ruling of the Commissioner of Internal Revenue (T. D. 2739) which holds that the tax imposed by said section upon the sale of automobiles and other enumerated articles is not applicable to such articles when normally exported. It seems to me that the two taxes, while of a somewhat different nature, are both in essence taxes on sales of certain products as such, subject to the same reasoning as respects the distinction between export and domestic sales. Unfortunately, however, the Commissioner of Internal Revenue has not yet ruled that the tax provided for in section 406 of the act of 1916 should be computed on the basis of domestic sales only. For this reason, I think it desirable to bring to the attention of your committee the effect of this tax provision as at present applied, with the thought that perhaps it will be found advisable to insert a clause in the present bill specifically exempting export sales from the imposition of the tax in question.

As an instance of the possible working of such a provision, if this is not done, I may cite the case of a very large manufacturer of cigarettes in this country, whose total output is exported, not a single cigarette being sold in this country. The tobacco consumed and the labor and materials used in the manufacture of the cigarettes are entirely domestic, and the industry is therefore one that might be considered a very desirable adjunct to this country. The larger part of the company's output is sold in China, where it is meeting very strong competition from Japan, one of the big disadvantages of the domestic company being the increased cost of transportation. The price at which the cigarettes may be sold to the average Chinese consumer is, as you can readily imagine, one that allows of a very slight profit, and this small profit is only overcome by the amount of sales.

If the present provision in the revenue bill under consideration by the Finance Committee should go into effect, this company would have to pay at the rate of 6 cents for every thousand cigarettes or fraction thereof exported, or in the neighborhood of \$100,000 per annum. This additional burden is so great that it might be the cause of transplanting the industry from this country to China or some other country where the taxation is not so heavy. In the event that such should happen we should not only lose a very profitable portion of our export business and a market for a large part of home-grown tobacco and six or seven thousand employees, but also the revenue resulting from the operations of the company in the nature of stamp taxes, income taxes, and other tax charges. I appreciate that this is an extreme instance, but it seems to me that the effect of this tax on our total export business is likely to be quite considerable.

As of possible interest in this connection, I hand you herewith a copy of Commerce Reports, issue of August 22, 1918, and call your attention to the article on page 720 thereof, which indicates the competition from Japan that our manufacturers of tobacco and tobacco products are already meeting in China.

Very truly, yours,

THURMAN,
Acting Secretary.

HON. F. M. SIMMONS,
Chairman, Finance Committee,
United States Senate, Washington, D. C.

Mr. MARTIN. There is one paragraph that I would like to read from the Commerce Reports (reading):

INCREASING TRADE IN JAPANESE TOBACCO.

(Excerpt from Japan Advertiser of July 18, transmitted by Consul General George H. Scidmore, Yokohama.)

The tobacco trade of Japan in China and some other Asiatic countries is believed to have a fair prospect in spite of formidable competition. The rate of increase since the war began is apparently a support of this belief.

The export of Japanese tobacco is principally made through a company organized for that purpose and the principal market is in China and the South Pacific. Leaf tobacco has been so far favored by foreign buyers, but the shipment of cigarettes is increasing rapidly, and sometimes Chosen has to be drawn on to make good the shortage in domestic goods.

As to the prospect it is said by a tobacco man that in China the British-American Tobacco Co. holds a controlling position with its offer of better

tobacco, and Japan seems to have no chance to improve its position, but the prolongation of the war is seen to be in favor of Japan. With the further reduction in space for tobacco, foreign goods will come on the market less actively and Japanese goods may wedge in. Japanese hope that in a year or two Japanese tobacco will hold China's market equilly with foreign goods; that it may even outrival foreign goods.

The CHAIRMAN. Is there any other gentleman who desires to be heard this morning?

Senator DILLINGHAM. Mr. Chairman, I would like to submit this letter from the Estey Organ Co., to be copied into the record.

The CHAIRMAN. Very well.

(The letter referred to is here printed in full, as follows:)

ESTEY ORGAN CO.,
Brattleboro, Vt., September 4, 1918.

Hon. W. P. DILLINGHAM,
United States Senate,
Washington, D. C.

My DEAR SENATOR: Will you permit me to state a few facts and opinions in reference to the proposed tax of 10 per cent on the selling price of pipe organs?

Pipe organs, as you know, are to a very large extent installed in churches and are an essential part of the public worship.

The usual procedure in the purchase and installation of a pipe organ is a long process, ordinarily beginning with agitation among the members of the church for improved musical worship, resulting in a subscription and campaign among the members for the raising of funds. Sometime early in the process the manufacturer of pipe organs is consulted and a fairly definite plan is mapped out as to the requirements of the church and the fund to be raised to meet that requirement.

I will not burden you with attempting to go into the details of this, as undoubtedly you understand it, having had experience probably in this matter. In short, a fund is usually raised and an organ bought accordingly.

Pipe organs are manufactured and sold on a very small margin of profit. Our experience, extending over many years, has shown us that there is considerably less than 10 per cent profit over the net cost of production and at the present time it is a very difficult matter to make cost and price meet. In many instances, owing to increased cost of material, our experience shows a decided loss on individual sales.

It is evident that the manufacturer can not carry a 10 per cent tax on the selling price of an organ and it will have to be ultimately passed on to the public, and in view of the way funds are raised for the purchase of organs, it seems more than likely that a tax of 10 per cent will practically kill the organ business in this country during the war, as it would be most difficult to go back to the communities and get them to raise additional funds under present conditions.

A very large proportion of the skilled craftsmen employed in the production of church organs are men advanced in years. The majority of our best mechanics are men of from 50 to 60 years and over. These men can not readily adapt themselves to other work.

It does not seem to me that it is an exaggeration to assume that church organs are to a certain extent essential to the national welfare and interests of the public, on account of the use to which they are put.

I would not think of making a protest against a tax of musical instruments in general, but I believe church organs should not be placed in this class.

I do not know whether you would care for a schedule of figures, showing cost of production and selling prices, but if it would be of any benefit, I shall be glad to supply them. Of course I would have to make the figures up from my own experience, as those would be the only ones available to me.

I shall greatly appreciate your bringing this matter to the attention of the Committee on Finance when they are considering the new revenue bill.

I am, very respectfully,

J. E. ESTEY.

The CHAIRMAN. If there is no one else who desires to be heard, the committee will stand adjourned until to-morrow at 10.30 o'clock a. m.

(Whereupon, at 12 o'clock noon, the committee adjourned to meet at 10.30 o'clock a. m. to-morrow, Tuesday, September 10, 1918.)

TO PROVIDE REVENUE FOR WAR PURPOSES.

TUESDAY, SEPTEMBER 10, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10.30 o'clock a. m., in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present: Senators Simmons (chairman), Smith, Thomas, Jones, Gerry, Nugent, Penrose, Lodge, McCumber, Smoot, Dillingham, Townsend.

The committee resumed consideration of the bill (H. R. 12863) "to provide revenue and for other purposes."

The CHAIRMAN. We will hear Mr. A. F. Thomas this morning. Mr. Thomas, whom do you represent?

INCOME TAX.

STATEMENT OF MR. A. F. THOMAS, OF LYNCHBURG, VA.

Mr. THOMAS. I represent no particular interest in this matter.

Senator PENROSE. To what phase of the bill do you address yourself?

Mr. THOMAS. The income tax.

Senator PENROSE. Are you an attorney?

Mr. THOMAS. No, sir.

Senator PENROSE. In what business are you?

Mr. THOMAS. I am interested in manufacturing.

Senator PENROSE. What kind of manufacturing?

Mr. THOMAS. The manufacture of wagons. Mr. Chairman, in looking over the list of distinguished Senators who compose this committee, I feel particularly fortunate in having such a forum in which to present my cause. I can not undertake to impress you with authority, but shall try to appeal to your reason, to your sound judgment, to your common sense, to your patriotism, to your democracy and your republicanism, because those two terms in their general sense are synonymous.

I shall crave the indulgence of this committee for permission to present the matter I have in hand in an uninterrupted way.

Senator THOMAS. How much time do you want?

Mr. THOMAS. I think it will take about an hour and a half.

The CHAIRMAN. We can not allow you that.

Mr. THOMAS. I am perfectly willing to begin the reading and leave the committee to decide as to the time.

The CHAIRMAN. We have not thought of giving any one person any such time as that. We would not get through these hearings in six weeks if we did.

Mr. THOMAS. I am perfectly willing to accept the judgment of your committee in that matter. If your committee thinks proper to stop me at any time, I am entirely willing to stop.

The CHAIRMAN. I think, in view of what you have said, that it would be better for you to fix a time, because we would not want to interrupt you in the middle of your discussion. We want to give you ample opportunity to present your views concisely, and you will present them more concisely if you are limited than you would if you thought you were going to have an hour and a half.

Mr. THOMAS. As I said before, I am here—

The CHAIRMAN. I do not think we can hear you more than half an hour. That is as much time as we have given anybody.

Senator THOMAS. How many of these gentlemen present expect to be heard to-day? We have quite a number of gentlemen present and they may be here for the purpose of being heard to-day. If that is the case, Mr. Chairman, we can not give anybody half an hour.

The CHAIRMAN. I have requests here from only six.

Mr. THOMAS. I have devoted a great deal of time to the study of this question. I have taken up the governmental and economic sides of this question, and I have not yet met anyone who is familiar with the income-tax question who thinks it can be presented in 20 minutes.

Senator THOMAS. I may say that some of the members of this committee have devoted a few hours of their time, during the past four years, to studying this question, and also in paying tax under it, so we know a little something about it ourselves—just a little, not much.

Mr. THOMAS. I have not the slightest doubt that you know a great deal about it. At the same time, I have these views, and if the committee wish to hear me, I should be very glad to present them.

Senator PENROSE. I assume the gentleman can be permitted to file a brief.

The CHAIRMAN. That has been stated repeatedly.

Senator PENROSE. But it is ridiculous to expect the committee to listen to any one man an hour and a half on any phase of this bill. If we did, it would take six years to get through with it.

The CHAIRMAN. Of course, Mr. Thomas, as Senator Thomas has just said, the committee understands something about this, and we do not wish an academic discussion of this question. We want a practical discussion of the bill as we find it written, your objections to it, or your advocacy of any particular part of it, and we think that if you will make an effort to condense your views you can probably say in substance everything that you want to say to us in half an hour; and that is all we want—a direct, concrete statement of your views.

Mr. THOMAS. Mr. Chairman, if you will allow me, I think I could present what I want to present in the time we are taking in discussing the whys and wherefores of it.

The CHAIRMAN. I will give you half an hour from this time, and we will try not to interrupt you any more.

Mr. THOMAS. I will take that, and just let the committee decide at the end of the half hour whatever they wish to do.

Senator THOMAS. We have decided it right now. At the end of half an hour we are going to hear somebody else.

Mr. THOMAS. That will be all right with me, Mr. Chairman.

Senator THOMAS. It will have to be.

(Mr. Thomas thereupon read to the committee from his brief, printed at the end of his statement, during the reading of which the following occurred:)

Senator SMOOT. Whatever you say, I take it for granted you have in that paper. What I would like to do would be to have you now submit your paper to be printed in the record just as if you had delivered it, and then I would like to ask you a few questions; and I think we could get more information that way, because we read your paper anyhow, which is what you want. It is not the mere question of taking up time.

Mr. THOMAS. No; I have no desire to take the time of the committee.

Senator SMOOT. You have only a few minutes more, and I will ask you to let me ask you some questions, because I want to get some information.

Mr. THOMAS. I will yield to the wishes of the committee in the matter.

Senator SMOOT. No; your wishes.

Senator PENROSE. I would like to remind you, Senator Smoot, that we are all very busy men; some of us have been on this committee 20 years and studied the thing pretty carefully, and an academic paper does not interest the committee very much.

Mr. THOMAS. I thank you, Senator, for the suggestion. At the same time, I feel that there are some things that the committee might hear to its advantage.

Senator PENROSE. You have not advanced a proposition that I have not been familiar with for the last 15 years. I say that respectfully to you.

Mr. THOMAS. If the committee desires that I should discontinue the reading of the paper, it is all right with me. I want to put before you, however, before you ask a question, the remedy I propose, in a few words.

Senator SMOOT. Very well. But I would like to ask you a few questions.

Mr. THOMAS. I should be very glad to answer your questions if I can.

Senator THOMAS. You can put your manuscript in the record, and we will read it.

Mr. THOMAS. I have no pride of authorship, and I will submit it any way that will suit you. I want to say that the principle which I undertake to explain in there is that the income of the country has been selected as the subject of taxation, and under any system you may devise it takes a certain percentage of that income. You can not help that. That is obliged to be a fact.

I notice Mr. Kitchin in his report estimates that at \$10,000,000,000. To raise the revenue that is wanted from that source will take a uniform tax on business profits of about 33½ per cent. As I say in that paper, under the systems they propose the tax ranges from

four-tenths of 1 per cent under one plan to 37 per cent on certain cases cited by the Secretary of the Treasury. Under the war-profits plan it ranges from 1 per cent to 56 per cent.

I hold that if you tax the sum of these profits, the tax should be uniform; that every business should be required to pay the same part of its net earnings that other businesses are required to pay; that there should be no differentiation in the rate of business taxation. It should be the percentage upon the whole. I suggest, in order to meet the views of the Secretary of the Treasury, to assist along in the sale of bonds, that you place a normal tax of 10 per cent on income and an excess tax or supertax of 30 per cent on income, which would be equivalent to a uniform flat tax of 37 per cent on incomes.

Senator SMOOT. What is your idea as to exemptions?

Mr. THOMAS. None.

Senator SMOOT. None at all?

Mr. THOMAS. No. All business, both individual, partnership, and corporate, would come under that, and no exemptions from it at all, except perhaps a nominal arbitrary exemption to eliminate inconsequential incomes.

Senator SMOOT. Amounts it would not be possible to collect?

Mr. THOMAS. To seriously affect the situation.

Senator SMOOT. That would cost more to collect than they would amount to?

Mr. THOMAS. Yes.

Senator THOMAS. Would you exempt benefactions to hospitals and schools and other public institutions?

Mr. THOMAS. That would come in the nature of arriving at the income, and I would exempt those charitable institutions. That does not come in the tax plan. My idea was a uniform tax, and then, of course, reasonable exemptions under the general plan. That is a detail. I would exempt, and I think there ought to be exempted, all gifts for public purposes; that is, of a public nature. I would exempt anything that happened to be for war purposes, whether direct or indirect, as it is a governmental purpose. All beneficial and charitable enterprises should be exempted.

However, I see in the bill a provision that I think is rather broad there. In the Kitchin bill I notice that they exempt all income of corporations organized for charitable purposes. A good many of them may be run on their income, and not on these donations, and the effect of that would be to increase the endowment. I do not know; I have not had time to examine it, and have not had the opportunity. But it may be that some of those corporations are so organized that they may be disorganized and become the property of the people who started them. In that case they would furnish a most convenient receptacle for income taxes until the clouds blow away.

The CHAIRMAN. Your time has expired.

Mr. THOMAS. Mr. Chairman, I am perfectly willing to get out of the way.

Senator SMOOT. Leave your brief with the reporter.

Mr. THOMAS. Yes, sir.

(The brief submitted by Mr. Thomas is here printed in full, as follows:)

INCOME-TAX LEGISLATION.

By A. F. THOMAS, Lynchburg, Va.

Thomas Payne opened his brochure "The Crisis" with the memorable observation, "These are the times that try men's souls," which is entirely applicable to our present situation. It is patent even to the casual observer that the United States of America has assumed world leadership, with its tremendous power and equally tremendous responsibilities. History offers no parallel; past experience dwindles into insignificant incident; there is no trail to follow; we must blaze the way as we go. Never since the dawn of human history has the world been confronted with such gigantic problems, upon the correct solution of which depends the hope of future well-being. The situation presents a ringing challenge to the leaders of the world, and never before was there so great need of patriotic purpose and constructive ability of the highest order. The Congress is undertaking to do that which has never been done before on so tremendous a scale. It has wisely, I think, determined to apportion the burden of this war, so far as possible, between the present and the future, and perhaps never before has a larger percentage of the costs of similar undertakings been put upon a cash basis. I have no criticism to make either of the purpose or the judgment displayed in making this division. It is generally understood that it is the purpose of the Congress to raise \$8,000,000,000 by taxation, a large part of which is to come from business profits and personal income. The question before the Congress to-day does not touch this purpose. It is conceded that the amounts desired from these sources can be raised by either of the methods that have so far been suggested and, therefore, the problem before us is not one of providing revenue. The task at hand is to provide a method of equitable apportionment of the burden between the individuals and units of business that must meet these large demands of the Government. To stress the point: The thing to be done is to provide a method of taxing business and personal income that will conform to sound economic principles and be essentially just to the different taxpayers.

It has been estimated that the business of the country will receive this year an income of something over \$9,000,000,000, out of which the Government, if the method is fair, can collect the amount required without seriously interfering with the efficient conduct of business. It is more important just now to concern ourselves with the effects which a particular method may superinduce than to consider the amounts to be paid by any particular taxpayer or class of taxpayers, for of all times the present and the immediate future are least opportune to invite industrial and financial disturbances.

With the total amount of revenue needed assured, Congress can well afford to devote its attention to the economic and sociological effects of the methods proposed before enacting them into law. He who assumes that the conduct of the war and the provision for funds to pay its costs are the only essential factors, has only a partial conception of the situation and should be reminded that when the great purpose to which this Nation has unreservedly committed its lives and fortunes has been accomplished and the peace terms shall have been dictated by the allies at Berlin, there will still remain the problems of reconstruction and readjustments that will call for the best statesmanship of all the world if our hopes of democratic development are to be realized. The point is that we should not only provide a method of raising the necessary revenue, but what is of equal and perhaps of more importance, we should so provide it that the operation of the plan will be in consonance with the demands of justice and sound economic principles.

Discussion of income-tax legislation suggests a division of the subject into taxation of business income and taxation of personal income. The principles applying to these classifications are different. The method which with entire propriety might be employed for one of them would not be permissible for the other. It is to be said, too, that income taxation in this country is as yet in an embryonic state and there is, therefore, the greater reason that the groundwork of the system should be well considered now in order to avoid unfortunate results in the future. Empiricism is always risky and sometimes dangerous. It is well, too, to stress the fact that the income tax is a highly efficient instrument which can be used with equal facility to promote well-being or to rob

mercilessly the class against which it may be directed. It is opportune, too, to point out to the rich and powerful that the misuse of power by them to secure favors would establish an extremely dangerous precedent which may be used against them at some future time when perchance they no longer shall be so potent in shaping the public policies of the Nation. Being most vulnerable on account of having most to lose, it behooves them to do their utmost to insure the legitimate and just use of this instrument of taxation. Clearly in their own interest, they should seek no special favor for themselves nor willingly submit to the adoption of any plan that conferred it upon others.

TAXATION OF BUSINESS INCOME.

Business, whether conducted under the individual, partnership, or corporate form, is a social instrument. Society permits it in order to get the service it renders. Conducted under private initiative it is a privilege, the conditions of which it is peculiarly the duty of government to prescribe. The public good is the standard by which the legislature should be guided in limiting its operation or restricting its opportunities. The Government in taxing it uses it as an instrument to collect the tax from the public it serves. It is a modern application of the Chinese and Roman customs of farming out the taxing function. A tax upon business whatever form the imposition may take is an excise tax on privilege. If it is made a tax on net earnings the theory assumes that the net earnings of the business of the country is a unit, and from this sum of business profits a certain percentage is taken for public use. Not only is this an assumed theory but it is a practical fact. Even Congress with all its power by any device, however ingenious, can no more alter this result than its enactments could make 2 plus 2 equal 5. What it can do is to devise a plan for apportionment of the tax between the different units of business equitably or inequitably. In the past it has done it inequitably, and if certain proposed methods are adopted it will make the division of the burden still more inequitable.

It must be understood that business is not a taxpayer. It is a tax shifter. Without a clear understanding of the principle of tax diffusion it is hardly possible to arrive at a satisfactory conclusion on the subject. Business under private initiative is dependent upon profit for its growth, capacity for service, and its life. Without it it must cease to serve and die of inanition. Profit being its lifeblood whatever lessens it becomes at once a matter of vital concern. Business seeks to lessen expense, to keep taxes at the lowest rate, and to increase earnings in every permissible way, and sometimes in ways that are not justifiable either in law or morals.

That the power to tax is the power to destroy is perhaps more true of business than other things. As soon as the tax imposed becomes too heavy to shift with facility business like a tired beast begins to slacken its speed, and if the burden it made sufficiently heavy it will stop altogether. Manifestly, then, the wise, prudent, and just thing to do is to place upon business a tax that will yield all the revenue possible without lowering its productive efficiency and further to provide a plan so equitable that each separate business will only be called upon to surrender for public use a just proportion of its earnings.

Having selected, as the income tax does, the profit fund of the country as the subject of taxation the capital invested furnishes no standard by which to measure the amount of the tax, because there is in this case no fixed relation between the different capitals and earnings. The earnings themselves furnish an exact, definite, and just standard leaving neither justification nor excuse for the adoption of any other. If we, hypothetically, grant that capital invested should be used as the measure of tax obligation, common justice would require that the exact capital of each taxpayer should be ascertained. This would necessitate Government audit of every business in the country beside which the ascertaining of the physical values of the railroads would appear as a holiday diversion. To accept less than such an audit would put a high premium upon every stock-watering scheme that has been foisted in all the past upon a gullible public. If anything approaching a fair and just system of taxation is to be realized the use of capital invested or prewar earnings as a standard of tax obligation can not be permitted. The fact that I would impress upon the committee is that neither the war-profits plan nor the excess-profits plan is anything more than an excise tax on profits.

The objection to both of them is not that they tax profit but that their standards are incorrect, producing an inequality of apportionment of the tax between the respective taxpayers that is unsound, unfair, and unnecessary. The war-profits plan with a flat tax on so-called war profits aims to restrict the tax to that part of the profit fund derived from business during the war that may be in excess of profits obtained at some period anterior to the war, while the excess-profit plan undertakes by exemption and graduation to take so much of the profit fund as may not under the method be found to be a permissible profit. Both are similar in selecting only a part of the profit fund rather than all of it for taxation. Both fail to grasp the broad principle that justifies the taxation of business profits.

Profit is social tribute. It is the price that society pays for its deficiency in organization. Whether the public reaches it through price regulation or an excise tax, it is the attempt to minimize the exaction to the extent that the public good may require. Upon this ground the restrictive action may go even to the extent of destroying all profit and thereby destroying the business if the public good is subserved. It may be fairly assumed that all business permitted to operate, to the extent of such permission, is necessary to efficient production and therefore that there is no legislative purpose, either by retardation or acceleration, to regulate commercial and industrial enterprise by discriminatory taxation. If then the purpose is to use business as an instrument for the collection of revenue and it, in order not to interfere with economic operation or lessen productive impetus, is to be disturbed as little as possible, it is highly desirable that the tax should not be in excess of that which may be shifted with facility to the consuming public. The importance of the point here demands perfect frankness.

Whenever the tax is made sufficiently large to endanger that which the manager of the business may believe to be a necessary return to take care of the possible losses, the normal growth of the business, and an satisfactory return on capital, business activity will begin to wane. If, too, the method of taxation is faulty giving some businesses advantage over others it degenerates into legislative sabotage, throws a monkey wrench into the Nation's industrial and commercial machinery, and insures the abnormal success of the favored class with a corresponding destruction of those adversely affected by the discrimination.

Both the war-profits and the excess-profits plans are faulty in this respect, as I shall demonstrate later on.

Both of the above plans profess to be hot on the trail of that elusive character the "profiteer," whose identity, so far, has not been definitely determined, except that his name is Human Nature and he has something to sell. It does not seem to alter the case whether the article for sale is a bag of peanuts, a day's labor, the products of mines, the factory, or the farm.

WHAT IS PROFITEERING?

Before undertaking to use the power to tax for correlative and punitive purposes it is proper to ascertain the true nature of the evils to be reached and to inquire further whether the good results reasonably to be expected from the proposed remedy will likely compensate for the undesirable effects that may follow its application. Let us analyze present profits to see if they are altogether what they seem: In the first place we must realize that money standard, whether of dollars, pounds, francs, or marks, is not a measure of value. It is only a means of expressing the ratio of values. It fluctuates as these ratios change. Weight and measures are standards of actual value.

The pound of meat, the bushel of wheat, and the yard of cloth remain the same, however much the values as expressed in money may change. These values are the same now that they were before the war, hence to ascertain the real change that has taken place or to ascertain the increase in the percentage of profit one must not only compare the nominal profits of the antewar period with those of the present, but must translate both of them into actual values as expressed by weight or measure, and the difference between the two profits of these periods so expressed will be the increase or decrease of the respective periods.

To illustrate: If the profit-and-loss account for 1913 shows a credit of \$100,000, while that of 1918 shows \$200,000, the difference expressed in dollars would be an increase for 1918 of \$100,000, or 100 per cent, which would make

the business fairly eligible to the conscienceless profiteer class. We find that the following articles have advanced since 1913 approximately as follows:

	Per cent.		Per cent.
Steel.....	140	Spring steel.....	220
Lumber.....	100	Cotton goods.....	200
Oils.....	100	Common labor.....	100
Bolts and rivets.....	275	Corn.....	150
Malleables.....	113	Wheat.....	100
Steel axles.....	210		

Groceries, meat, etc., the Lord only knows how much. If the average is taken, it will be found that the larger nominal profit of 1918 will not purchase as much of these real things as the smaller profit of 1913. Hence, the business profits increased in nominal value but decreased in real value. In other words, the purchasing power of money has been reduced more than half since 1913. This change of standard under which prewar debts, salaries, and fixed incomes shrink while most other things soar ushers the world into a fool's paradise in which it disports itself in a way that would do credit to Bedlam.

While there are many elements entering into the proposition, the main reasons for the decline in the purchasing power of money will be found to be the enormous destruction of property, the tremendous inflation of currency, and the unprecedented use of Government credit in practically all countries. So long as the war lasts there seems to be no reason to expect any improvement in this respect, and while it continues a constant readjustment of nominal values will be necessary, and neither Government regulation nor price fixing without dangerous interference with production can stop the upward trend of prices. This change of nominal values is the effort to preserve the parity of values and it affects everything which human desire has called into existence.

Business in addition to the profit necessary to insure growth and furnish incentive must have an insurance fund sufficient to protect it against probable and even possible losses. This charge is increased as the risk increases except that the tendency is to increase it even more rapidly than the risk, hence hazardous business carries a larger percentage of profit than that subject to less fluctuation.

Now, when we consider that nominal profits are based upon large inventories of goods at inordinately high prices subject to large diminution of nominal value when the inevitable reaction takes place and further that these losses can not be transferred to consumers in a falling market, who can say until the full cycle of inflation and deflation has been completed which business has profiteered and which has not?

No claim is made that people are not profiteering so far as they can. If accomplishment of the purpose is to be the deciding factor in the ascertainment of guilt, the case can not be decided until the record is made up, while if the purpose to get all one can is to be the test, it is to be feared there will at no time be a sufficient number of innocents abroad to apprehend the guilty.

I hold no brief for the profiteer. He who would purposely take advantage of the necessitous conditions incident to the war to oppress others or to weaken the hands of the Government no doubt deserves all the obloquy which his misdeeds will bring him. Neither am I an advocate of the doctrine of laissez faire in this matter. Society, by the most effective method available, should protect itself against such antisocial practices. I do not oppose the use of the taxing power for corrective or even punitive purposes. The income-tax principle rests upon the theory that this power shall be so used.

As already explained, business is a social instrument, and even if the income-tax method is used in imposing a tax, the tax itself is essentially an excise tax on privilege. Corrective or punitive taxation should not be imposed upon business, because it is not the most effective way to reach the desired end and because it will likely produce economic effects more detrimental to society than the evils it is intended to cure.

The still stronger reason that taxation of business should not be the instrument employed to correct profiteering is that there is a simpler remedy, which will effectually reach the real ultimate profiteer without seriously interfering with productive efficiency and will at the same time strongly incite to greater economy in unessential expenditure, thus conserving the economic forces of the Nation.

Instead of belaboring and crippling the machinery of production, as a discriminatory tax on business would do, the more effective plan would be to reach

out and take hold of the real culprit, the owner of the machine—the individual who is the beneficiary of whatever undue exactions business may have made upon the public. Leave the business machine well supplied with all the support necessary to its highest efficiency and let it have an unimpaired and constant incentive to work, but when the excess of its earnings has been passed to the individual owner, the taxing power can lay its hand upon it and take by a method of graduated taxes so much as the need for revenue and the public welfare may require. The difference in the effects of the two policies will be the difference between national prosperity and national disaster.

THE PROPOSED PLANS.

The setting aside of the profits of any period anterior to the war on the theory that they represent the normal earnings of the business in existence at that time can not be justified. It assumes that there existed at the particular time selected a fixed ratio of earnings, an established relation between the different businesses that was just and equitable and should therefore be preserved. Upon this premise rests the justification of the plan that having once assured to the different businesses their just share as ascertained by the prewar standard, the Government can in fairness call upon all to surrender as taxes 80 per cent of all earnings in excess of the prewar amounts. Superficially the proposition may appear plausible and fair. The premise that there is or ever was a fixed and invariable ratio of earnings between the various businesses of the country is entirely at variance with the facts of the case not only at the prewar period selected but at all other times. No such static condition in the relation of earnings has ever existed, and in the very nature of business never can exist. Business activity, efficiency of operation, and resultant earnings are constant only in their inconstancy. Like the waters of the sea, they are constantly rising and falling. If the simplest form—two businesses engaged in identical effort—is taken as an example, it will be found that their earnings bear no fixed relation to each other. The profitable business of this year, by a mere change of the personnel of the management or alteration of some other of the many possible circumstances, may become the unprofitable business of next year, or the losing business of this year, by some change of method or fortunate circumstance, may become the highly profitable business of next year. The assumption that there is at any time a fixed relation between businesses as regards their separate earnings ignores entirely the varied ebb and flow of general business, as well as the continual readjustments that affect materially the earnings of the separate units. Arbitrary interference in the operation of economic law is at all times risky, and unless very carefully and wisely done will usually result in serious harm. It is, indeed, going a long way and unduly tempting Providence to say that a fixed, arbitrary standard of relative earnings for the thousands of different businesses of the country shall be established. It is evident that the business caught in the low tide at the time of fixing its status must remain henceforth under a terrible handicap, while that which may be in its high tide will have vouchsafed to it an advantage that will be destructive to its less fortunate competitors.

The establishment of this false, economic status under the operation of a revenue law calling for an exemption of an amount equal to the established prewar profit and imposing an 80 per cent tax on the amount in excess of it necessarily establishes a differential in favor of well-established and highly profitable businesses as against those which were less developed and less profitable during the prewar period. In effect, the effect of this plan would be to tax the strong and fortunate less and the weak and unfortunate more. The constant effect of the plan would be to eliminate the weaker and less fortunate units of business and to make more secure the position of the stronger. We have heard of the insidious secret rebates in freight and all are familiar with the destructive effect of the same on those against whom the practice was directed. I do not hesitate to say that the effect of the operation of this proposed revenue plan would make the work of the inventor of secret freight rebates look like the crude efforts of a novice. Once put the plan into operation and assure its continuation and the weaker elements of commerce and industry might as well place above their doors the inscription that Dante found above the portals of the Inferno. The point is that it does not so much matter with these fortunate, large prewar earning factors whether the plan makes them pay more or less taxes than some other plan. The thing that must appeal most to them is that the operation of the plan gives them an economic advantage over their competitors that in the end will enable them to destroy them. If the case was permitted to rest here it might be answered that it was a matter

of opinion, and that others of even superior judgment as firmly asserted that such effects would not follow. Fortunately, the case is not dependent upon mere opinion, but is susceptible of exact mathematical demonstration.

	Per cent.
A's prewar earning.....	20
A's present earning.....	30
Less 80 per cent of excess.....	8
Leaving net earning of.....	22
Percentage of net taken for taxes.....	26½
Remaining to A, 73½ per cent of earnings.	
B's prewar earning.....	10
B's present earning.....	20
Less 80 per cent of excess.....	8
Leaving net earning of.....	12
Percentage earning for taxes.....	40
Remaining to B, 60 per cent of earnings.	
Differential in favor of A, 13½ per cent.	
Again:	
C's prewar earnings.....	100
C's present earnings.....	200
80 per cent tax on excess.....	80
Leaving net earning.....	120
Percentage of total earnings left.....	60
D's prewar earnings.....	50
D's present earnings.....	200
Less 80 per cent on excess.....	120
Leaving 80 per cent of earnings.	
Percentage total earnings left, 40 per cent.	

Hence C retains 20 per cent more of his total present earnings than D, illustrating that the 80 per cent war profit plan in reality is a progressive scale of taxation so graduated as to put the highest rate on the lowest prewar earning capacity and a decreasing rate as the prewar earning increases. Expressed differently, the more one earned in the prewar period the smaller per cent of present earnings he is required to pay as tax, while the less he earned in the prewar period the more of the present earnings he is required to surrender; from which it becomes plain that if a business, struggling under sharp competition, inefficient management, or serving the public humanely at the lowest reasonable profit made a meager profit in the prewar period, it would now be destructively handicapped as against a greedy management that exercised quasimonopolistic powers to maintain profits at a high level during the prewar period. It is said that God tempers the wind to the shorn lamb, but if this plan of taxation is adopted it will remain for the American Congress to temper it to the wolf.

What has so far been said may be thought to be matter of opinion, but fortunately we have an official expression embodying figures taken from Government records. The Secretary of the Treasury filed a memorandum with the Ways and Means Committee of the House illustrating the practical operation of the present law, the war-tax plan, and the excess-profits plan, from which I have made up the following table showing in approximate percentages the operation in the cases cited:

Name.	Net income.	1917 excess tax.	Per cent.	War-tax plan.	Per cent.	Excess-profits plan.	Per cent.	Capital invested.
B Co.....	\$34,459,103	\$5,780,580	16	\$16,523,004	48	\$7,568,174	21	\$138,011,107
C Co.....	21,123,848	6,257,808	29	13,600,536	36	9,028,602	37	70,826,677
D Co.....	15,956,478	515,921	4	175,118	1	65,969	0.4	157,845,797
F Co.....	37,366,210	5,256,610	14	14,767,436	39	5,538,088	14	190,009,155
G Co.....	10,091,678	1,322,472	13	3,655,175	36	1,371,095	13	51,683,519
H Co.....	3,308,967	211,742	7	234,195	6	88,121	2	31,032,232
I Co.....	5,131,800	799,152	15	2,182,692	42	884,399	17	24,034,647
L Co.....	17,539,197	2,604,511	15	7,497,950	42	3,333,025	19	77,502,479
M Co.....	7,945,057	1,611,325	20	3,191,531	40	2,430,100	30	22,103,694
N Co.....	7,542,741	607,993	8	1,601,100	21	759,761	10	30,982,015
O Co.....	9,496,274	645,850	7	1,129,504	12	790,291	8	69,599,705
Q Co.....	6,251,757	896,465	14	2,476,430	39	1,139,048	18	28,374,706
X Co.....	7,992,433	1,081,185	13	2,943,137	37	1,123,329	14	62,490,120
Total.....	186,358,561	27,847,667	15	69,942,118	37	34,040,303	18	.....

Before discussing this table it may be proper to recall that the war-profits and excess-profits plans differ principally: First, in the method of ascertaining the exemption. Waiving the arbitrary exemption of \$3,000, the first bases it on prewar earnings, or 10 per cent on capital invested. The latter gives exemption of 8 per cent on capital invested.

Second, the first imposes a flat tax of 80 per cent on the taxable part of the income, while the latter imposes a graduated tax of 35 per cent on the taxable income not in excess of 15 per cent of the capital invested, 50 per cent on the taxable income not in excess of 20 per cent of such capital, and 70 per cent of such taxable income as may be in excess of 20 per cent of the capital invested. The war-profits plan in so far as the prewar earning standard of exemption may apply, discriminates in favor of all businesses having a large prewar earning capacity to the extent that such earnings exceeded 10 per cent on the capital invested. The excess-profits plan (and the war-profits plan, also, when the percentage of capital invested method is used) discriminates in favor of the most inflated capitalizations. The prewar-earning method rewards the business that has been most merciless in its exactions upon the public in the past, while the capital-invested method extends its highest favors to the business which has most flagrantly falsified its capital. Under both plans he who has fraudulently capitalized on a basis of 4 of water to 1 of capital and exercised monopolistic power to compel the public to pay exorbitant prices that yielded 8 per cent on this false capitalization would escape taxation.

To illustrate:

Actual capital.....	\$20,000
" Water ".....	80,000
Supposed capital.....	100,000
Prewar earnings.....	8,000
Present earnings.....	8,000
Exemption, war-profits plan.....	10,000
Exemption, excess-profits plan.....	8,000
No taxable income.	
Actual capital.....	20,000
Earnings \$8,000, or 40 per cent.	
If honestly capitalized, this operation would still escape under the war-profits plan, but under the excess-profits plan would pay as follows:	
Net earnings.....	\$8,000
Less \$3,000 and 8 per cent on capital, \$1,600 equals.....	4,600
Subject to tax.....	3,400
Tax, 70 per centum.....	2,380
	1,020
Plus exemptions	4,600
Net left business.....	5,620

Equaling flat tax of 30 per cent on net income.

This demonstrates clearly that in the contemplation of these two plans the real hardened, wicked profiteer is only he who did not mercilessly fleece the public during the prewar period or he who failed to foist successfully upon an overtrustful public a financial organization false in essence and dishonest in intent. The temptation to characterize such methods of taxation is strong, but respect for this presence and the limitations of parliamentary language make it inadvisable.

Reverting to the table, it will be observed that neither in the present law, the war-profits plan, nor in the excess-profits plan is there anything approximating uniformity of results. In the cases cited the percentage of net income taken by the present law ranges from 4 per cent to 25 per cent; under the war-profits plan, from 1 per cent to 56 per cent; and under the excess-profits plan, from four-tenths of 1 per cent to 37 per cent. Upon what principle can we justify permitting one company to retain 99 per cent of its net income, while another is left only 46 per cent? By no stretch of the imagination can a plan that gives such results be called a tax system. It is a practice of arbitrary exaction that would do credit to the old barons of the past.

While the results shown in these cases are bad enough, I am satisfied that the worst is not known and that a more complete examination and analysis of

Income returns would demonstrate even more conclusively the inequality, imperfection, and utter lack of proper standard in both plans. It will be noted that the table shows that the average tax under the present law on the income cited was only 15 per cent of the net income, while under the war-tax plan, with its rates varying from 1 per cent to 56 per cent, the amount named can be secured by a uniform rate of 32 per cent. The excess-profits plan, with its rates ranging from four-tenths of 1 per cent to 37 per cent, can get the amount asked by imposing a uniform rate of 18 per cent.

Why, then, should Congress resort to methods that are demonstrably incorrect, when the straight, simple way of equality and justice lies in plain view?

Is there any hidden virtue in complexity and indirection that they should be chosen when a better way is at hand?

Is conferring special benefits upon some by imposing hardships upon others commendable statesmanship or even good morals?

The proposed plan, involving the ascertainment of the capital invested, should be discarded not only because it is an incorrect standard and that it is practically impossible to ascertain the facts but likewise because it increases tremendously the difficulties of administration. The present bill provides for the creation of a board to assist the department interpret the law. Recently the commissioner requested an extra appropriation of \$25,000,000 to increase his auditing force and at the same time expressed the opinion that it would take the auditors he now has two years to complete the work of auditing the 1917 returns. Much of this work results from unwise and unnecessary provisions in the revenue act. Simplification is the remedy. The creation of the proposed board would be an admission by Congress of lack of simplicity and clarity in the law. The most satisfactory tax law is that which deals uniformly and fairly with all taxpayers and is so clear in its intent that little is left to construction and interpretation. In this, as in other laws, the judge's discretion is the beginning of injustice and maladministration. If the rigors of the law are to be softened by quasi judicial action, the strongest will get the most favors, and this will be true regardless of good or bad intentions. The necessity for the complexity of the law and its consequent difficulties of administration does not appear. I am not prepared to admit that the hands of our statesmen have lost their cunning or that faith in the efficacy of simple, democratic principle is on the wane. When we dismiss extraneous purposes and become willing to direct our effort to the sole purpose of providing a fair and efficient tax law we can discern more clearly the principles involved and greatly simplify the method of administration.

ECONOMIC ASPECTS.

The welfare of a nation largely depends upon efficient production and just distribution of wealth. While the former is vital to the life of the nation in war, it is of paramount importance even in times of peace. No apparent gain of present revenue would justify the enactment of any provision of law that would have the effect of diminishing production. Neither would a law having this effect be advisable, even from a temporary point of view, because it would at once begin to reduce the volume of things out of which revenue must come. It should be realized that taxation by any method must confiscate the things now in existence. The Government has but two alternatives, either to get revenue out of the current production or to get it out of the reserve created at a former time. So long as the exaction is taken from current production at a rate that leaves sufficient incentive to the worker to continue production, it need not necessarily lessen the national wealth, but if it is sufficiently large to absorb the present production and infringe upon former production the Nation has commenced its march to bankruptcy. While this is true in a general sense, it is equally true in special relation, and, therefore, if a tax method is unequal in its application, and those discriminated against are placed in a position of having an undue proportion of their wealth taken, this class will decline in productive efficiency in the proportion that the exaction is improper. Who will say that A, being allowed to retain only 44 per cent of his current production, has the same incentive to produce as B, who is permitted to retain 99 per cent? In the last analysis, the income tax as applied to business is the confiscation by the Government of a given part of the production remaining of that which was produced in the tax year, and every consideration of justice and the effect of economic law demand that the confiscation shall take place by a definite, uniform rule that compels each to contribute his share. The tax should be definite. Business will adjust itself

to any reasonable conditions when once they are known, but if the highest efficiency is to be maintained these conditions must be clearly manifest. Nothing is more detrimental to business efficiency than uncertainty. Once started business to watching the clouds and the wheels of progress begin to slow down at once. The strongest incentives to production are hope of reward, a desire to serve, desire to make a success of one's efforts, etc. As applied to business under private initiative, all these are concentrated in profit, because upon the ability to get it hangs the possibility of all the rest.

Under the war-profits plan, when profits shall have reached the amount of the exemption, the operator can only hope to receive one-fifth of the additional gains. If an additional volume of \$100,000 is done on a margin of 15 per cent, the business will retain, after paying the tax, the sum of \$3,000, or 3 per cent on volume. Who believes that a business man of average judgment would undertake a contract promising a maximum possible profit of \$3,000 and run the risk of losing perhaps five times the amount?

In these times of highly inflated prices, the chances are largely in favor of the latter supposition. The effect reasonably to be expected of such a plan is a general slowing down of business activity, and when the additional fact that the exemption feature of the plan establishes an arbitrary, false economic standard of business is considered it becomes evident that the effects of such a tax will be disastrous. It should be borne in mind, too, that an 80 per cent tax is too large to be shifted with facility, and therefore the only safe thing for a business to do would be to make the amount exempted and then curtail business all possible in order to avoid taking risks which the probable return would not justify. It may be that some board sitting like guardian angels in Washington assisting the Treasury Department may extend the saving hand to some drowning business of sufficient magnitude to arrest its attention and enlist its sympathy, but the great body of injured taxpayers suffering under this incongruous measure will not likely locate the source of their trouble until after their economic efficiency has been impaired and bankruptcy has given the coup de grâce. There is nothing better established than that rapidly declining returns superinduce caution, limit business, and lead to stagnation. The war-profits plan, except in so far as its exceptional favors to false capitalization may help such businesses, will likewise have a disastrous effect upon the Nation's business. The operator's return in excess of the exemption by short steps falling from 65 per cent to 50 per cent and then to 30 per cent of the excess net earnings will surely not incite business activity, but, on the contrary, will have exactly the opposite effect.

If on the other hand, identically the same amount of tax was to be collected and a uniform rate of taxation were adopted, it could be done without serious economic effect. In the first place, the rate would be uniform and need not be other than reasonable. Based on nine billion income, it would be one-third of the income. A proportion which business could bear without serious result. This method would not superinduce any relative changes in the economic status of the different business units of the country, but would place them all under the same relative obligation, leaving them otherwise free to maintain or better their relative positions as industry, good judgment, and fortunate circumstances permitted. I repeat that the exemption, whether based upon prewar profits or percentage of capital, under both plans not only assumes a fixed status of earnings for all businesses but actually establishes this status. All earning in excess of these fixed amounts are treated punitively. Both plans undertake to crystallize all business units and definitely fix their relative earning powers. The effort to establish a fixed status of business earnings by law will be about as effective as were the commands of King Canute calling upon the tides of the ocean to recede. We would do well to learn the lesson that he intended his apparently foolish act to teach.

The effects of such a policy would likely induce the decline and disintegration of those businesses which, at the time of fixing the status, were in unfavorable positions as to earnings or capitalizations. It matters little to a particular business what the definite tax rate may be if it is only given time to adjust itself to it, provided it is given a slight differential over its competitors. The natural trend of all business is toward monopoly and the more discriminatory the laws the more rapid the progress toward the goal. It may be well to remind those, if there are any, who would hurry the economic evolution that the law of compensation has neither been repealed nor is it repealable, and that the admonition, "that which thou sowest, the same shalt thou reap," is as true in economics as it is in morals.

The forces of evolution, as never before, are driving the world forward from the competitive to the cooperative basis. It will tax to the utmost the powers of all to make the necessary readjustments. The economic changes are proceeding at tremendous speed.

Why should any reasonable man desire to increase it still more?

Under these circumstances, is it advisable or prudent to launch out into untried economic and sociological experiments, especially when they are apparently unwise and plainly unnecessary?

As a remedy for profiteering, both plans are without merit. As tax measures, they accomplish the purpose in an illogical, unjust way, and view from the point of economic effect they are positively a public menace.

THE REMEDY.

Destructive criticism is one thing; constructive suggestion is quite another. I would not feel that I was fully justified in indulging in the one if I could not offer the other:

The business income of the country is a definite, determinable thing. This unit is composed of the earnings of all the different businesses of the Nation. The proportion of the whole that the law takes for public purpose is the exact proportion that each business of the country should contribute of its earnings. If, as has been estimated, the net income of the business of the country for 1918 is \$9,000,000,000 and the Government desires to secure \$3,000,000,000 of revenue from this source, it is manifest that a flat tax of $33\frac{1}{3}$ per cent would yield the desired sum. I suggest, however, out of abundant caution to insure the full amount of revenue and a further desire to assist, as far as it can safely be done, the sale of Liberty bonds that a normal tax of 10 per cent and an excess tax of 30 per cent be imposed upon all business income, which would equal a flat tax of 37 per cent. This would yield, assuming a \$9,000,000,000 income, \$3,330,000,000 of revenue.

This provides for no exemption on business income and assumes that all business income whether derived from individual, partnership, or corporate operation will be uniformly treated. There should be no exemption, except perhaps a small arbitrary exemption given for the purpose of eliminating the inconsequential incomes. It is manifest that the exemption of a percentage of the earnings would be of no use to any taxpayer, since it would only result, if the same amount of tax was to be secured, in uniformly raising the rate. The uniform treatment of all business income is suggested, as it falls under the same principles, and there appears to be no sound reason for the separation of individual and partnership business income from corporation business income, as is proposed in the House bill.

The method here suggested is simple, direct, and determined. The taxpayer knows the 1st of January what he may expect. It leaves him to work under a uniform, continuous incentive. He must surrender 37 per cent of his earnings, and he retains 63 per cent. He is under the same incentive to work in December that he was in January, and therefore the tax so levied if the rate is reasonable will act as a constant spur to increased production rather than a deterrent, since the operator will realize that he can hope to make up for his loss in taxes only by more economical operation and increased volume of production. The plan is fair and just to all. It neither seeks to punish nor reward anyone. It is scientific, conforming to a definite rule, and therefore will not have to be changed each morning to meet the demands of passing whims. It will serve for all time with only such change of rate as the changing circumstance of the public need for revenue may make advisable. It will serve notice upon both plutocrat and sans-culotte that no favors are to be expected.

It will greatly simplify administration. It will have nothing to do with capital invested nor with prewar earnings. It will only be necessary to ascertain the current income to arrive easily at the tax. I have earnestly endeavored to show that the use of prewar earnings and the capital invested was only a standard by which to measure the amount of the taxpayer's obligation; that is to say, to arrive at the part of the present income that he must surrender to the Government. The simpler plan here suggested avoids all this complexity and goes straight to the income itself—an exact determined thing, and makes its relation to other incomes, likewise definitely determined, the standard of obligation. This method is scientific and mathematically exact and leaves no ground for the charge of unjust discrimination.

PERSONAL INCOME.

The income-tax principle applies peculiarly to individual income. In theory it is a process of equalization. It finds its reason in the assumption that some have gathered where they have not sown to the deprivation of some and to the detriment of the social whole. As a mere method of taxation it is faulty in that it does not make a demand upon each to contribute according to his ability to pay, but leaves untouched both the property of him who is too shiftless to increase his talents and that of them whose circumstances make this increase impossible.

All personal income may be divided into two classes—earned and unearned or service income and investment income. The first does not come under the income-tax principle in its equalizing aspect so long as the income is commensurate with the personal service. Personal service is here intended to mean the actual work of the individual whether this service be with brain or brawn, or both.

The Senator receiving the pittance of \$7,500 per year for his arduous and oftentimes unappreciated labors, and the coal baron or oil king spending his time in diversion while drawing millions on account of the ownership of the economic machine, furnish brilliant examples of the two classes of personal income taxpayers. It is manifest that these two classes do not occupy analogous positions. The individual has a right to the product of his labor, and in justice can only be called upon to pay the part that he owes as a member of society to support the Government which was instituted for social benefit. The tax, if correctly adjusted, is a debt which he can be called upon to pay without any invasion of his individual right to possess what he produces. It follows that a tax upon service income should be made to conform as closely as possible to an equitable apportionment among the taxpayers of the amount necessary to meet the public needs. This principle would require a uniform rate on service income. Viewed in its practical aspects, it would seem that in a scale of graduated taxes on personal income, service income should be placed in the lowest brackets.

Unearned or investment income comes fully under the income-tax principle in its equalization feature. The individual investor, unlike the individual worker, has no prescriptive right to any return on his investment. This return is the product of privilege, and society through its government has the right and the power to restrict or limit it to any extent. Whether this return is left large or small or is entirely eliminated is purely a matter of public policy. The economic effect of both graduation and restriction of this income is quite different from that following the same treatment of business income. In the latter case it has a direct effect on production, whereas in the former it would not affect production at all, but on the contrary would have a salutary influence in curtailing nonessential expense. The greatly reduced return from investment will usually cause the investor to retrench.

The most pronounced economic effect would be the diminution of the investment fund in individual hands. Whether, as Mr. Carnegie was reported to have said, that it is better to have the most of the investment funds owned by a few, or, as some contend, that the country is best off that has its surplus wealth most widely scattered is a question which it is not necessary to discuss at this time. It is apparent that the Government at the present time needs the surplus funds of the country more than anyone else, and the great extension of enterprise under its initiative leaves little room for that of the individual. The taking of the surplus income from the individual by the Government simply diverts it into another channel. In so far as this fund would have been invested in Government bonds the immediate economic effect of taking it for taxes will be nil.

I have never attached much importance to the popular cry of "Catch the profiteer," realizing that but few understand the real questions involved. As an economic proposition, all business profit stands on the same footing. The difference is one of degree and not of kind. It, whether large or small, is a social tribute that privilege exacts for doing for the public that which it has not as yet developed communal sense enough to do for itself. The effect of taking profit from the public depends greatly upon the use that is made of it. Productive use of it is in a large way beneficial, while its dissipation in non-essential expense is a public loss.

We have now pursued the analysis far enough to point with certainty to the receiver of investment income as the "man higher up," the last and ulti-

mate profiteer, for whatever has been or still may be done of profiteering is for his exclusive benefit. Having at last tracked him to his stronghold and identified him beyond the hope of escape, we turn him over to that avenging Nemesis, the Congress, with an earnest prayer that God may have mercy on his soul.

Aside from sociological reasons for limiting investment income to prevent the acquisition of the industrial and commercial mechanism of the country by the few, thus establishing a régime of private monopoly, sufficient reason exists in the public need for funds to justify a heavy graduated tax on investment income. It can not be said that any investor receiving after taxes are paid an annual income sufficient to provide for reasonable personal needs had been compelled to suffer very great personal privation. If the Government needs the money, there does not appear to be any valid reason why all receiving large investment incomes should not be compelled to surrender whatever may be in excess of their reasonable personal requirements. Their sacrifice is certainly not comparable to that of our boys who have left home, friends, and business to risk their lives upon foreign soil to sustain principles in which every American worthy of the name is vitally interested.

SUGGESTED CHANGES IN THE REVENUE BILL.

Section 230 (A). "In the case of a domestic corporation 18 per cent upon the amount of the net income in excess of the credits provided in section 236: *Provided*, That upon so much of this amount as does not exceed the amounts distributed to shareholders during the taxable year the rate shall be 12 per cent," etc.

It is apparent that the language here employed does not convey the true intent of the framers of the law. It is evidently the purpose of the proviso to allow a rate of 12 per cent on all income distributed to stockholders, but the language used restricts the 12 per cent rate to such amount as may have been distributed during the taxable year, or, in other words, the distribution must take place on or before the 31st of December of the taxable year; that is to say, that corporations reporting as of December 31 for the taxable year of 1918 could not avail themselves of the 12 per cent rate on the amount of dividends paid in January, 1919. I suggest the following change: "*Provided*, That upon so much of this amount as does not exceed the amounts distributed of the income of the taxable year to shareholders prior to making the return for the taxable year the rate shall be 12 per cent," etc. This allows corporations a reasonable time after making up their annual statements to arrange for dividend distribution.

There is serious objection on economic grounds to the policy of putting a premium of 6 per cent upon the distribution of earnings. Even the most superficial thinkers will admit that the public good will be subserved by keeping the industrial, financial, and commercial machinery of the country in a state of high efficiency so that it may continue to function normally. Whatever may be the idea entertained of the initiative under which the operations should take place, all reasonable men will agree that the bull in the china shop method can only produce public disaster. It is generally recognized that business safety is best insured by carrying proper reserves and this policy becomes increasingly important as the element of risk increases. With prices and credit extended far beyond the danger point, with certain reaction before us, the extent of which none can foretell, there is every reason for the conservation of business resources to enable it safely to weather the coming storm. Common sense and a proper regard for future welfare call to us in no uncertain tones to prepare against the dangers of the reconstruction and readjustment that will surely follow the cessation of this war. Under such conditions, it would seem to be the height of unwisdom for Congress to put a premium upon digging under the foundations of the pillars of safety. If it is thought advisable to induce the distribution of earnings it should in all events be limited to amounts not in excess of one-fourth or one-half of them.

Section 214 (11). It is not entirely clear that corporations are allowed these deductions. This provision appears to be defective in that it is too broad in some respects and too restrictive in others. It is doubtful if the deduction of gifts to all such corporations should be allowed as they may operate on their income while the gift would go to increase endowment. This fact, coupled with the possibility that the foundation or institution, although doing scientific and charitable work, might, in effect, be the property of private parties or re-

vertible to them, suggests that it might prove a ready instrument for defrauding the Government out of income tax. It should be made clear that both individuals and corporations may deduct gifts to recognized war funds, such as the Red Cross, Y. M. C. A., etc., since such donations are plainly for a governmental purpose.

Not having seen the full text of the bill, the discussion of these provisions does not commit me to the approval of others.

SUMMARY.

No question of raising requisite revenue is involved since either of the methods will accomplish this purpose.

Business is a social instrument necessary to the normal and efficient progress of society. Under private initiative it is a privilege to be registered as public policy may determine. Business taxation is an excise tax and should be so imposed as to interfere as little as possible with efficient operation and maximum production. It should be uniform to the end that each unit of business will be compelled to bear its relative share of the public burden. It should not exceed the amount that business can shift to the consuming public.

The objections to the war-profits and excess-profits plans are that their standards of measurement of tax obligation are unfair, unjust, and unnecessary. That they set up an arbitrary economic status of business earnings entirely out of accord with the facts, and that the result of such enforced status will operate as a powerful instrument of discrimination and destruction against the weaker elements of commerce and industry; that the effect will be to foster and encourage private monopoly and become a propelling force of tremendous power to hurry unduly and dangerously the economic evolution that is already moving with great rapidity. There is no necessity for such dangerous and doubtful economic and sociological experiments as these tax methods involve because there is a simpler, more just way that will apportion the tax equitably among the taxpayers and at the same time have a minimized effect upon production. This plan greatly simplifies administration and makes unnecessary any reference either to past profits or capital invested. This method consists in making net earnings the measure of tax liability and imposes a uniform tax upon them, thus insuring a reasonable tax rate that all can bear without destructive effects.

If profiteering is done, business is only the instrument, while the individual owners of it are the real beneficiaries, and that Congress has full power by a graduate tax on personal income to reach each of them and appropriate whatever of their incomes that public policy and the public need for funds may make advisable.

The effect of heavy taxation of large personal incomes will not affect production unfavorably but will superinduce greater economy in unnecessary personal expenditure.

THE GENERAL SITUATION.

The world has reached the end of an epoch. A new one is now being born. Man had no power to prevent the one nor has he ability to cause the other. He is forced along in the current of happenings that is now rushing onward toward that far off divine end, the true nature of which human imagination can not fully grasp. With all its untoward events, this age is one in which it is a great privilege to live, and especially is this true of us Americans. The final struggle between autocracy and democracy is taking place to decide as it must whether power concentrated in the few or diffused among the many shall be the method of human cooperation, whether men shall be brothers or the greater part of them be slaves. If democracy proves the stronger in the contest, of which I have no doubt, its principles will become all pervading and permeate the political, industrial, and social world. The changes that this will make necessary will be fundamental and revolutionary. The United States will have the opportunity to become the moral leader of the world if only we develop the character and capacity necessary to this exalted position. To do this, opportunism and selfish purpose must be thrown aside, and our acts, our conceptions, and our ideals must be brought into conformity with those fixed principles of equality, uniformity, and fraternity that form the bedrock foundations of democracy. To you, gentlemen, members of the highest legislative body in the world, comes with peculiar force the call to take the lead and

shape our destinies and those of the world; not that you, however able or powerful, can thwart the final purpose, but you may direct progress along pleasant paths rather than have remorseless evolution force us again to undergo the tortures of that hell through which selfish and short-sighted mankind is now groping its way toward the light.

(The chairman here submitted a statement from the National Tax Association, which is here printed in full, as follows:)

PRELIMINARY REPORT OF THE COMMITTEE ON FEDERAL TAXATION OF THE NATIONAL TAX ASSOCIATION.

The undersigned committee, appointed by the executive committee of the National Tax Association, conceiving it to be of immediate importance to secure the views of the members of the association and such others as might be led to join in the movement, on the principal questions involved in the preparation of the pending Federal revenue bill, prepared and distributed a questionnaire inviting responses. While the conduct of this inquiry has developed many interesting and valuable suggestions, it is evident that many members have found themselves engrossed in war activities and otherwise so busily engaged that they have been unable to give the time and attention to the matter as speedily as it was hoped would be the case. The canvass will therefore be continued up to the time of the final report which will be made to the St. Louis conference to be held November 12.

In view, however, of the considerable number of carefully prepared responses coming from all portions of the country comprising the views of members thoroughly posted on the subject, and especially in view of the immediate activities of the congressional committees in considering pending legislation, it has seemed desirable to issue this preliminary report giving the results of the canvass up to this time.

In presenting this report the committee considers it important to make it as brief and concise as possible and therefore confines itself to those questions which have been susceptible of an affirmative or negative reply, omitting those involving explanatory or argumentative matter, although many such would be of interest and value were it possible to report upon them. For the same reason it has seemed inappropriate to comment upon such replies as might be done to advantage in bringing out more clearly their meaning and intent and stating any qualifications expressed.

It is assumed that the members of the association, the congressional committees, and the Federal officials may find some value in the mere results of the canvass in view of the character of those participating.

Replies have been received from 90 members, coming from 27 different States, including 22 economists, 39 business men, 10 lawyers, 13 State and local officials.

Not all questions were answered by everyone and only those results are given in which a fairly large number of replies were received.

From our knowledge of the character, standing, and experience in tax matters of those replying, it is believed that the replies may fairly be considered as conveying the general opinion of the country at large upon the questions, many of which are of difficulty and have obviously required no little thought and study.

The committee takes occasion to express its deep appreciation of the cooperation which has been thus extended and of the patriotic and unselfish manner in which the answers have been made.

The questions selected for report with the replies are submitted herewith on attached statement.

THOMAS E. LYONS,

Wisconsin Tax Commission, Chairman.

PROF. FRED R. FAIRCHILD,

Yale University.

A. E. HOLCOMB,

American Telephone & Telegraph Co.

GEORGE E. HOLMES,

Attorney at Law.

O. C. LOCKHART,

Ohio State University.

SEPTEMBER 18, 1918.

Result of canvass of replies to questionnaire of committee on Federal taxation of the National Tax Association received up to Sept. 19, 1918.

Question.	Answer.	
	Yes.	No.
ADMINISTRATION.		
1. Should there be simplification and a consolidation of the various taxes upon a given taxpayer under one act?	69	7
2. Should regional boards be established at various convenient points throughout the country for the administration of income and profits taxes?	42	20
3. Should such boards be independent of the Treasury Department?	13	27
INCOME TAX.		
4. Should the exemptions of \$1,000 and \$2,000 be lowered?	32	39
5. Should the entire income above a certain amount be taken as tax?	14	56
6. Should salaries of State officials and income from State securities be taxed? (Reference was made to the recent cases of Peck v. Lowe and U. S. Glue Co. v. Oak Creek in 247 U. S.)	51	12
7. Should the attempt be made to tax "unearned" income at a higher rate than "earned" income?	44	25
8. Should the income tax on corporations as such be continued (the alternative being to tax the shareholders)?	38	22
9. If practicable, is the taxation of undistributed income justifiable?	31	15
10. Would you advise the insertion of a provision preventing in the future the making of contracts by one to pay the taxes of another (applies particularly to "tax free" bonds and "tax free" rentals)?	11	12
11. Should stock dividends be treated as income?	43	27
12. If the income tax is continued on corporations should the present provisions taxing dividends received be continued?	7	27
13. In such case also should the limitation on interest deduction be continued?	12	21
14. Should gains from the sale of capital assets be taxed at the same graduated rates applicable to current income arising from the use of capital?	38	21
15. Should steps be taken to promote international comity with respect to taxation of nonresident citizens and corporations and of aliens?	38	11
PROFITS TAX.		
16. Should the present excess-profits tax law be continued?	39	.....
17. Or should a war-profits tax based on the British system be substituted?	26	.....
18. Should an alternative method be provided, the taxpayer to pay the higher amount of tax whether it be computed as an excess-profits tax or as a war profits tax?	19	.....
19. In arriving at the profits tax, should an attempt be made to give some allowance to special industries?	40	2
20. Should the present discriminatory 8 per cent tax on salaries and other "earned" income be retained?	6	44
21. Should the present method of determining "invested capital" be changed?	30	.....
EXCISE TAXES.		
22. Should the present excise taxes be increased?	28	2
STAMP TAXES.		
23. Do you favor stamp taxes on checks?	30	46
24. Should stamp taxes on other documents be imposed?	25	27
ESTATE TAXES.		
25. Do you favor Federal estate taxes?	35	21
26. Should the present rates be increased?	15	12
POSTAL RATES.		
27. Do you approve of the existing increased postal rates?	44	18
28. Do you approve of the special postal rates on advertising?	49	15
CUSTOMS DUTIES.		
29. Should additional customs duties be imposed?	26	19
30. Should discriminatory duties be levied against enemy belligerents?	12	30
LUXURY TAXES.		
31. Should taxes on luxuries be imposed?	58	7
32. Should taxes on articles of general use when used as luxuries be imposed?	38	7
CONSUMPTION TAXES.		
33. Should taxes be levied on articles of general consumption—i. e., tea, coffee, sugar, etc.?	41	26

The CHAIRMAN. The committee will be glad to have the views of Mr. James W. Kinnear.

STATEMENT OF MR. JAMES W. KINNEAR, OF PITTSBURGH, PA.

Senator SMOOT. In what business are you engaged?

Mr. KINNEAR. I am a manufacturer.

Senator SMOOT. Of what?

Mr. KINNEAR. Of munitions and steel—tool steel. Gentlemen, I am not before you as an expert; I am just an ordinary business man. People of the United States expect to be taxed; they want to be taxed enough to do this thing right. We only expect you to fix it so that it will bear on us all equally; that is all.

The feature I am especially interested in is the feature of the relief of moneys given to charities—educational, benevolent, and religious. What you did last year was an innovation in tax law so far as I have been able to find out. I have just come from London a few weeks ago. While there I met some men of affairs, and when I told them what Congress had done here they said, "We wish we had some such a relief here on money given away," and I have no doubt that the Parliament of England will follow very shortly what has been done here.

It was an innovation. You recognized the spirit of sacrifice which is abroad in the air, and is about the most beautiful thing as yet that has come from this war, and when men have stood up and wanted to give, give, give to these great causes, you have come forward and relieved them individually from taxation. I am here just to ask you to go one step further. When corporations want to do the same thing, why should they not be relieved? The corporations have souls, notwithstanding the ordinary sentiment that they have not, and their directors and stockholders all over the country are willing to give. I know there are some lawyers on this committee, and all of you are aware of the fact that it may be contrary to law for the directors of a corporation to give. However that may be, it is being done.

I understand you do not want to seemingly approve anything that is not according to law. Why not, then, merely provide that where a corporation gives in a legal way that would be authorized by the stockholders, if that were necessary, where they give in a legal way, they shall be relieved from taxation? There is no reason why money that is honestly given, with a spirit of cheerfulness and sacrifice, should be, after it is given, also taxed. The amount of money that you are going to win for the great causes of this country by doing this is far more than the amount of tax you are going to get on money given by corporations.

Senator PENROSE. I saw stated in a recent article, I think in the Forum, by a gentleman whose name I do not recall, but who was an expert accountant, that the corporations holding a large number of these 10 per cent plus contracts have made large contributions to the Red Cross and other purposes and charged them up and got 10 per cent on that expenditure. Do you know anything about that?

Mr. KINNEAR. I do not see how they could possibly do it under the law.

Senator PENROSE. That is what this accountant says.

Mr. KINNEAR. They could not possibly do it unless they were guilty of deception.

The CHAIRMAN. You mean charging that up against the Government?

Senator PENROSE. A part of the expense of the corporation, together with lavish expenditures for wines, cigars, and banquets, and he gives a long series of scandalous expenditures.

Mr. KINNEAR. I have heard of that, too.

Senator PENROSE. He states this very positively. I do not think there is any doubt about it.

Mr. KINNEAR. It may have been done in cases, but you will find some people everywhere trying to evade the tax law. It has been since the days of Adam.

Senator PENROSE. The vicious feature of this is that he is getting 10 per cent on his alleged benefactions.

The CHAIRMAN. If that should happen, Mr. Kinnear, the Government would be responsible by reason of its negligence in not more properly examining and passing and auditing the accounts.

Mr. KINNEAR. Certainly; and they are doing that very thoroughly. Such corporations will be held up. They can not go on indefinitely with that method of procedure.

The one point I want to leave with you is that if you will relieve the corporations for money honestly and legally given, there will be more money provided for the great causes here than any tax you can put on that amount.

Senator THOMAS. I think we have not exempted them because they can not vote.

Mr. KINNEAR. Who can not vote?

Senator THOMAS. The corporations.

Senator SMOOT. And there are very few givers.

Senator JONES. What moral right has a corporation to devote its funds to charitable purposes?

Mr. KINNEAR. The stockholders of a corporation can do anything with the money that you can do with yours. It belongs to them.

Senator JONES. That is undoubtedly true. But what is the object in having the corporation give it rather than the individuals who are stockholders?

Mr. KINNEAR. That is owing to the conditions, Senator. The money in the treasury of the corporation is there, and it has not been distributed; it is there, and the stockholders will more willingly give that way than they will if it comes into their hands to give.

Senator JONES. Why will they?

Mr. KINNEAR. I can not answer why. That is a matter of psychology.

Senator THOMAS. Is it not a fact that that is the only way in which some of them can be induced to give?

Mr. KINNEAR. Yes; that is true.

Senator JONES. Then your proposition is that the controlling stockholders coerce the smaller stockholders to make contributions to some enterprise favored only by the controlling stockholders?

Mr. KINNEAR. I think the corporation giving would be unanimous. I do not think there would be any objection to it.

Senator SMOOT. It could not legally be done if any stockholder objected.

Mr. KINNEAR. No; I do not think so, because it is a matter outside of the ordinary line of business.

Senator JONES. Then, if you are going to get the consent of every stockholder, why not get up a subscription and have every stockholder sign it in proportion to his holdings in the corporation?

Mr. KINNEAR. Senator, you know that is intricate, and can not be worked out. Here you are in a stockholders' meeting, and here is a cause presented: "Are you willing to do this?" It goes through cheerfully and willingly; where, if I should go around with a paper and ask each one to sign, it would be very difficult.

Senator JONES. It has been my observation that in practically all such instances as you refer to, it simply means coercion of the minority stockholders.

Mr. KINNEAR. I think this, Senator, that the money that is given to-day is given largely by the directors, and it would be a good deal better to have it come down to the stockholders, from your point of view, than to have the directors giving it.

The CHAIRMAN. Where the directors give money, do not the stockholders have to approve it?

Mr. KINNEAR. I think in nine-tenths of the cases where the directors give it, it is approved by the stockholders, informally, but not in any formal way. If this tax is put on in the way I suggest, it would have to be done formally.

Senator SMOOT. The way two corporations, in which I am interested and am a director of, do, is to give it right out with the understanding that if there is any objection to it on the part of the stockholders—and so stated in public—the directors will make the amount good; and, up to this date, there has been no objection.

Mr. KINNEAR. There has not been any objection.

Senator McCUMBER. That is coercion.

Senator JONES. Yes; it is coercion.

Mr. KINNEAR. I understand, then, that the real objection in your minds is that you feel that the stockholders would be coerced into giving. That is it, is it?

Senator JONES. I do not think there is any doubt but what that is a fact. You take all the contribution by all of the corporations, and the result of it is the coercion of the minority to contribute something to enterprises favored by the majority.

Mr. KINNEAR. Then, practically every offer that is made in public, where the people hesitate to get up and speak, is the result of coercion, because that is the way money is solicited in large quantities. It is by the spirit of giving that is generated by one giving and another giving.

Senator JONES. It is tolerated by the minority stockholders simply because they are not strong enough to protect their rights without expense and trouble not commensurate with the evil which they must bear.

Mr. KINNEAR. Senator, I do not see it in that line. The stockholders are doing a great many things all of the time, and according to your theory—

Senator JONES. I think it is all wrong all the time.

Mr. KINNEAR. According to your theory it would be oppression all the way through. I am speaking of business matters.

Senator SMOOT. I think that under the law Senator Jones is perfectly correct, and it amounts to this, that one Bolshevik owning \$100 of stock could virtually hold up a million dollar donation to the Red Cross.

Mr. KINNEAR. Gentlemen, I have finished.

The CHAIRMAN. I understand you are not suggesting any change as to the subjects provided in the bill?

Mr. KINNEAR. None at all.

The CHAIRMAN. The objects of charity.

Mr. KINNEAR. Not at all.

The CHAIRMAN. You simply suggest that we permit the corporation to do what individuals may do in this respect, provided that it is done by the consent of the stockholders?

Mr. KINNEAR. Practically so, or legally done. I thank you, gentlemen.

(Mr. Kinnear subsequently submitted the following brief, which is here printed in full, as follows:)

PITTSBURGH, PA., *September 16, 1918.*

The SENATE COMMITTEE ON FINANCE,
Washington, D. C.

GENTLEMEN: You were kind enough to give me a few minutes before your committee on Tuesday last in behalf of exempting corporations from taxation on money given for religious, charitable, and educational purposes to 5 per cent of the net income of the corporation.

I desire in a few words to reply to the two objections raised by members of your committee to the insertion of such a provision in the new revenue bill, and would ask that this paper be filed in connection with my remarks made before the committee on Tuesday, September 10.

The objections were as follows:

The first objection was that the board of directors as a rule make such subscriptions for their corporations, that this is illegal, and your committee would not insert a provision in the revenue bill which would seem to approve an illegal procedure.

In answer we would say, if the stockholders in a legal manner approved the subscription or at their annual meeting authorized the board of directors to distribute a certain percentage of the net profit to charities, etc., it would not be an illegal procedure, and the provision in the bill should only exempt corporation subscriptions for charitable, educational, and religious purposes, when the same are legally made.

Such a provision would have the effect of correcting all illegal methods of making corporation subscriptions to charities, etc.

The second objection was that, even if the corporation subscriptions were approved or authorized by the stockholders, their approval would be in a way coercive upon some stockholders who might not wish to make such subscriptions but would do so rather than enter an objection.

This objection is weak and there is a complete answer to it as follows: The stockholders are fully protected under the law and if they ignore or refuse to invoke such protection they alone are responsible.

The Senator raising this objection may have had the impression that a majority vote of the stockholders would be sufficient to legalize such subscription, but this being a distribution of funds out of the ordinary line of business of the corporation, it would undoubtedly require the unanimous vote of the stockholders to approve or authorize such a subscription.

Why, then, should your committee feel called upon to protect the stockholders of a corporation who have it within their power to protect themselves?

To say that the large stockholders of a corporation as a rule coerce the small stockholders into giving to certain charities in which the former are specially interested is not true. Such a statement belittles and misjudges the

big-hearted, generous business men who are running the corporations of this country and who keep its business pulsations throbbing from the Atlantic to the Pacific.

There are many reasons for exempting corporations from taxation on moneys legally given for religious, educational, and charitable purposes up to 5 per cent of their net income. Some of these reasons are as follows:

1. It is manifestly unfair to tax money given for public purposes of this kind, when the country depends upon the public to finance so many public benefactions in connection with the war. All legislation should tend to increase public benevolences rather than diminish them.

2. It is frequently just as necessary for a corporation to give to the religious, educational, and charitable institutions, especially in the vicinity of the works of the corporation as it is to build sanitary houses for the workmen. The latter goes into the expense account, but money given for the former must be taxed, although it is just as necessary and vital to the success of the company as the latter.

3. Corporations are the great money makers of this country. They will give more easily and in larger amounts than individuals, and this is a distinct advantage to great public undertakings, where large sums are especially required.

4. As a rule the man of small means gives more in proportion than the man of large means, but where the corporations contribute the large and small stockholder gives in proportion to their holdings and for this reason, refusal to insert a provision exempting from taxation corporation subscriptions in a way protects the large stockholder more than it does the small stockholder.

5. The corporations of this country have given millions of dollars during the past year to the great public religious, educational, and charitable undertakings in connection with the war in addition to paying their war tax. The revenue bill which you are now considering will greatly increase their tax, the insertion of a provision exempting them from taxation on money given to public benefactions would be a recognition by Congress of what these corporations have done, as well as an encouragement to continue. It will mean far more to the public welfare than any tax you may secure on the funds given for public benefactions.

There is no legal or moral reason why corporations should not be permitted to give to public undertakings and be relieved of taxation up to a certain amount of such gifts. It is a great deal better to give the corporations an opportunity to voluntarily dispose of some of their profits in this way than to force the same into the public treasury by drastic tax measures.

The insertion of a provision in the pending revenue bill exempting corporations from taxation on moneys given to public charities, etc., will result in a wonderful increase in the corporation gifts during the coming year, and hereafter the corporations of our country will become a great factor in sustaining all public benefactions.

Your committee is respectfully urged to insert in the pending revenue bill a provision which will exempt corporations from taxation on all moneys given for charitable, educational, and religious purposes up to 5 per cent of their net income.

Yours, truly,

JAMES W. KINNEAR.

INCOME TAX.

The CHAIRMAN. We will now hear Mr. Reed. Mr. Reed, I believe you represent the Investment Bankers' Association of America?

STATEMENT OF MR. ROBERT B. REED.

Mr. REED. Yes, sir.

The CHAIRMAN. And wish to speak as their representative?

Mr. REED. Yes, sir.

The CHAIRMAN. Is there anybody else who wishes to be heard as the representative of this organization?

Mr. REED. No, sir.

The CHAIRMAN. You are the only spokesman?

Mr. REED. Yes, sir.

The CHAIRMAN. How much time do you think you will require?

Mr. REED. In view of the desire of the committee to expedite matters to-day and the number of gentlemen present, I thought I would try, if the committee would give me that much, to devote 20 minutes to income-tax matters and 20 minutes to excess profits.

The CHAIRMAN. Can you cut that down to 10 minutes with each?

Mr. REED. Yes, sir.

The CHAIRMAN. I want to say right here that I do not think the committee cares to hear the hearing of any documents that can be printed in the record. It would be much more helpful to us if you would talk to us in a direct businesslike manner. I think we will understand you better, and will get better results from your statement.

Mr. REED. That is just what I wished to do. This association, as you know, is composed of dealers in securities, about 500 of them, all through the country. There are 10 representatives here of investment houses in different parts of the country, and the committee possibly will not wish me to read all their names, of the West, the East, and the South.

In addition to certain special provisions of the income-tax law which do affect securities as such, the investment bankers, collectively, have a very vital interest in the income-tax and excess-profits tax as a whole, in the effect which these taxes may have on the industries of the country, on the successful flotation at this time of liberty loans, and especially on winning the war, and on the conditions after the war. We have always worked on these matters from the public viewpoint primarily, in addition to the special matters in which we are interested, because they affect securities, and the first matter I wish to discuss is the question of direct taxation on the interest on municipal bonds. On that point our position is really representative, because dealers can buy and sell bonds at any price, and the proposal is to tax future issues of States and municipalities. If municipalities go to a 6 per cent level, they go off the market. That is primarily the problem of the municipality.

Senator THOMAS. Is not the problem whether the Government of the United States has any constitutional power to tax a State security or the security of any State subdivision?

Mr. REED. That is the question.

Senator SMOOT. Is that what you are going to discuss?

Mr. REED. Not the constitutional question; no, sir. I want to call attention first to the fact that practically all State and municipal issues are, by the action of the Capital Issues Committee, and most effectively by the cooperation of the investment dealers of the country, kept off the market now, except those which the Capital Issues Committee find compatible with the interests of the country, and they are running now at an average of less than \$100,000,000 a year. A great part of those—none of us know just how many, but issue after issue that we do know of—are made at the instance of the National Government to help in carrying on the war. One instance I have in mind is county roads to cantonments. I know one county road in Camp Grant, the waterworks outside of Camden, N. J., to supply the cantonment, and my attention was just called yesterday

to a new school building out in Toledo, Ohio, for trading purposes. A large part of the issues are for those purposes, and a large part are under statutes, which limit the borrowing rate to 5 or 6 per cent.

Generally speaking, the provision will not prevent the borrowing on these bonds. They will not diminish the demand of available capital, except in those few cases where the interest rate is limited by statute, and there you put an absolute bar against something that may be absolutely necessary.

In the opinion of bankers, therefore, this would not restrict the issue of bonds, but would undoubtedly depress the market of municipal issues, and may disturb quite generally the financial conditions, and have a very serious effect on savings institutions and others. Whether or not that will help the liberty bond market is a very doubtful question.

Just one thing I do want to say about the constitutional issue: At the bottom of the constitutional issue, at the forefront of the whole subject, is a political issue, and the Supreme Court is bound to recognize that political issue, even though we do not have every reason to believe that it already had formed its opinion on this question. That political issue is whether or not Congress, in proposing the sixteenth amendment, put something over on the States. Everyone knows that the State legislatures did not consider that it gave the right to tax the instrumentalities of the States, and everyone knows that the State legislatures would not give that right. That fact is so patent on the face of it that nobody can ignore it. If the States should wake up now and find that they had inadvertently given the Federal Government, for the first time in our history, the right to tax, generally or discriminatively, the agencies for creating the borrowing powers of the States, they would be very much surprised and outraged.

Senator THOMAS. I presume you are familiar with Senator Root's opinion on that subject?

Mr. REED. Yes, sir; and with Gov. Hughes's message. Gov. Hughes never expressed a final opinion on it. He said there was no assurance but what that opinion might be taken, and the State of New York accepted that amendment on Senator Root's opinion. That was followed by the State of New Jersey, the legislature of which, under a message from Gov. Fort, concurring with Senator Root, accepted the amendment.

I may say this, that the investment bankers do not oppose the tax as such. They feel that if there is occasion—and there may be—when State and municipal issues should be taxed, in great emergencies, that should be provided for by amendment to the Constitution, and that amendment to the Constitution should be so framed as to prevent abuse of the power given, which would not be the case with the broad powers asserted, to tax them at will.

Senator JONES. If we have power to levy the tax, you still argue against its advisability, because it will depreciate the value of State and municipal securities. Would not that argument go to the exemption of all taxes on Government bonds, the Liberty bonds, and would it not be just as applicable to one as the other?

Mr. REED. A sudden disturbance of the relative established values is the disturbance which I had in mind, and I also had in mind a

second point which I am just now coming to, a provision in this bill which does tax, unquestionably, vast amounts of outstanding municipal bonds, and which will undoubtedly seriously affect their value. I think it is an oversight. I think probably it can be corrected at the Treasury. But this committee ought to have their attention called to it. That is the second proposition on that subject.

Section 214 and section 234 contain this provision:

Interest paid or accrued within a year on indebtedness * * * In excess of interest received free from taxation under this title.

That is the only deduction of interest allowed under the bill either to the individual or to the corporation. It is manifest, of course, that you do not get a net income until you deduct interest on indebtedness.

A, an individual, with a gross income less other deductions of say \$8,000 a year, has a \$10,000 mortgage on his house or farm or a \$10,000 current liability in his business on which he pays \$600 interest. He owns \$12,000 4 per cent municipals, paying \$480 a year, and \$10,000 liberty 3½'s, paying \$350 a year. His taxable net income in fact is \$7,400, but under this provision he can deduct only \$120 of his interest paid if he holds municipals and only \$250 of his interest paid if he holds the liberty bonds. The result in each case is specifically that the interest received on the tax-free securities is added to his otherwise taxable net income. This taxable net income becomes in the one case \$7,400 plus \$480, the interest on the "tax-free" municipals, or \$7,880; in the other case, \$7,400 plus \$350, the "tax-free" interest on the liberty bonds, or \$7,750. He is taxed for both normal and surtax on his income from the tax-free securities and the method adopted is simply a mathematical camouflage. It works out that way in every case.

B, a bank, has \$500,000 deposits on which it pays interest. Its net income is \$60,000. It holds, and has held for some years, State and municipal securities paying \$2,000 a year. It also holds \$20,000 liberty 3½'s on which it receives \$700 interest. It can deduct its \$10,000 interest paid, less \$2,000, plus \$700, a net deduction of \$7,300. Its net income becomes \$52,700. It is taxed to the full amount on the tax-free securities at a tax-free price, and in particular let me add it bought the liberty 4½'s under the very positive assurance of law that they were free of the normal tax.

It is only necessary to say, as an absolute fact, that in the case of a bank— and there are many of them—which will pay the 80 per cent and 18 per cent on the amount, however small, that is undistributed, they will pay that 80 per cent on the interest which they receive from liberty 3½'s, plus 18 per cent on the balance, a net tax of 83⅓ per cent on liberty 3½'s, which they bought as tax free, and in the case of the bank, the same thing applies to the liberty 4½'s. We all know there was no such intention in the drafting of this proposal. The dealers in securities have never objected to it, and do not intend to object to it during the war. It is intended to apply to an individual or a business that borrows directly to buy tax-free bonds.

Senator McCUMBER. Do you mean to say that section does not intend what it really says?

Mr. REED. It does not. The present law provides for the computation of the interest on indebtedness, except indebtedness incurred in the purchase of tax-free securities.

It was thought, and probably is true, that that provision, without further amendment, is capable of evasion. I do not know that anybody has evaded it, but probably they have.

I may say this, that all of us, when we first saw this provision, thought it was all right, thought it merely answered that difficulty. We woke up in a few days and began to see what it meant.

Senator McCUMBER. I read it over once, casually, but I could not read it over in any other way except to find that it taxed $3\frac{1}{2}$ per cent Liberty bonds.

Mr. REED. You were much quicker in seeing it than the rest of us.

Senator THOMAS. Did you call the attention of the Ways and Means Committee to it?

Mr. REED. I called the attention of the chairman of the Ways and Means Committee to it several weeks before the bill was adopted, but they had so many things on their minds that they did not get around to it. We called the attention of the Treasury to it, and I expect to see Dr. Adams about it this week. It is there, and of course it must be corrected.

One very simple fact results from that. Outstanding municipals are driven out from investment institutions and banks, so far as they can get rid of them, into the hands of the wealthy individual, who is the only man who does not have to borrow; and that is one great fear in this whole situation, that the wealthy individual will buy them. They are offering them to him on a silver platter at 8 per cent. It shows the need of seeing where we are going to get off before we start.

The CHAIRMAN. What was that you said about the wealthy individual getting 8 per cent?

Mr. REED. He certainly will be able to get many issues at 8 per cent if this should remain in the law.

Senator THOMAS. You mean 8 per cent discount?

Mr. REED. Eight per cent interest; an 8 per cent rate. He will be able to get municipals very cheap.

Senator McCUMBER. Owing to depreciation?

Mr. REED. Yes, sir. The short-term municipal issues. They are in the banks and they are now being bought and have been bought at very attractive rates. It has been very necessary that they should be.

I have right here a little ad. I happened to take out an old paper this morning from the State of Georgia. There are 300,000 school-teachers' warrants. For what reason that may be, I do not know, but they run the schools through the year, and they have to do it on warrants—

The CHAIRMAN. Your apprehension is that if we imposed this tax it will depreciate the value of the bonds and the rich people would buy them up?

Mr. REED. Yes, sir; that is the thing the Government wants to look out for. But we want also to prevent the absolute wiping out of the value of these present securities. The greatest buyers are the savings banks. It is only necessary to mention them to know what that means. They have been compelled by law to buy this class of securities.

There is one income-tax matter that I wanted to mention to you briefly, and that is the absolute importance, if you want to get a very high rate of taxation, of producing some allocation and averaging up between the years. A man may have had a tremendous loss. His capital may have been impaired last year, and he has got to make that loss good. The English law recognizes that. A man may have a tremendous contingent liability outstanding which really is connected up with various sources of his income this year. He has got to put the money aside to meet that in February or March of next year. He will have to face that liability without any funds out of which to pay it.

On the excess war profits taxes, let me say, as has already been said, as to general principles we would try to confine ourselves to the House bill, and offer suggestions which may help a little in working out from that bill something more in accord with the desires and views of the committee, and what seem now to be the views of the Treasurer.

We all want to see this bill enacted before the election, and we are absolutely praying for a miracle that it may go through before the next liberty bond issue—

Senator THOMAS. The day of miracles is over.

Mr. REED. I am afraid so, Senator. Gen. Foch is working a few miracles, and possibly this committee may work one.

In many respects this bill is very superior to anything else that has been proposed.

The thing we want particularly to protest against, as our time is short, is the definition of investment capital, and particularly in the allowance of contingent property at its value at the time it is acquired, not in excess of the par value of the stock. We have heard a great many protests against any proposal to value corporations as they stand to-day. Under this bill you have got to go back and value them 10 or 20 years ago, or else your only alternative is this alternative: In nine cases out of ten it is their stock value, which means a tremendous favoritism to watered stock. We not only object to it, but we object to the destruction it brings about to the corporations whose stock is not watered, especially those which have been undercapitalized.

Investment bankers and their lawyers know something about the issues of stock for property. They know that property can be bought for half its value and capitalized at twice its value, and the capitalized value can go up, under successful management, in the course of years—

Senator PENROSE. Have you any suggestion to make on that point?

Mr. REED. Perhaps I should not have stated the objection so broadly—

Senator PENROSE. It is one of the most important things in the bill, and I recognize the infirmity of that provision.

Mr. REED. If the percentage basis were to be retained I think we would suggest, practically, as a general proposition, what the Senate committee had in one of its bills last year as to capital employed and these definitions to the Treasury and to the courts. But we might have something more concrete.

Our objection is to the capital percentage basis, to the increase in the rates. We believe absolutely in the war-profits basis, and believe that it is capable of successful adaptation to the business conditions of this country.

Senator THOMAS. Have you investigated the legal question of our power or the power of any legislative body to provide an alternative system of taxation—a system which gives the taxing authority the power to use the one or the other as it may think it can get more tax by the alternative method?

Mr. REED. I have not investigated the legality or constitutionality of it. I can see the possibilities of argument.

I do not want to take the time of the committee, but there is one general fact that I wish to call your attention to—

Senator THOMAS. I consider that one of the most important legal questions in the entire situation.

Mr. REED. It is getting, sir, very important.

Senator THOMAS. If we can adopt two methods we can adopt 30.

Mr. REED. If a man gets off under one he could get caught under the other. If he is under one, he stays there. It minimizes immunity and doubles the confiscation.

Senator SMOOR. Is it not an absolute fact that under excess-profits taxes it is absolutely impossible under any provision that can be drawn to make a tax equal upon all business, wherever you take capital into consideration at all, and with an excess-profits tax you can not reach a plant without taking capital into consideration, whereas with war profits you do not have to take into consideration that capital, the borrowed money or water stock, or anything; it is just simply to take the money?

Mr. REED. That is absolutely our view, Senator.

Let me say this, that it is also our view that the real reason that the war-profits tax has never obtained the general support of the country is that there has never been any elastic provisions in it which would enable the Treasury to reach the concerns which Members on the other side and some in the Senate and the country generally have said escape from paying the tax on war profits. You must reach them on some equitable basis. You must have the power to reach them, and then you have a complete measure which will stand under any proposition.

Senator SMOOR. You say the public has not approved. I think most of the business interests in this country have approved of a straight war-profits tax.

Mr. REED. I think that is true of the business interests.

Senator SMOOR. I have resolutions from nearly all the commercial bodies of the United States—I will not say all, but I have a great proportion of them, from the Atlantic Ocean to the Pacific.

Mr. REED. I think that is true as to the business interests, and their influence is properly felt; but it is not the only influence that is felt in Congress and in the press. There has been and there will continue to be, I think, opposition, and perhaps successful opposition, to the war-profits tax as a successful measure, unless it is tied up with broad general powers to reach the concerns that had their successful period in the prewar years.

Mr. Moore of Pennsylvania, in the House yesterday, made what on its face was a complete demonstration against the war-profits

proposal, and the factor that he ignored is the factor that I want to bring out here. He said [reading]:

There are two corporations each with a million dollars' capital and \$200,000 income. One made \$80,000 and the other \$200,000. We tax a man who was poor in the prewar period. We do not tax the man who was rich in the prewar period.

The man, in other words, who has been rich right along. The stock of the corporation in the prewar period was worth the proportion of \$80,000 to \$200,000—

Senator SMOOT. And rightly so.

Mr. REED. And they consider always that they are taxing one taxable owner when he is not the same man at all. Nine-tenths of the injustice under this proposal is due to the failure to recognize the fact that you are taxing the present owners of the property.

A and B, for instance, may have invested \$100,000 in 1900 in a new corporation, and that may be the invested capital under this act on which it is allowed to earn \$8,000 or \$10,000, and be taxed 35 per cent to 70 per cent or 80 per cent flat on the excess. C and D may have purchased the stock of A and B in 1914 for \$500,000, and though that is the capital invested by them in this property, they are only allowed to earn about 2 per cent upon it and are taxed 35 per cent to 70 per cent or 80 per cent flat on the excess above that 2 per cent. There is not a provision in this bill which would give them any relief.

Senator SMOOT. That is under the excess profit; and you can not get away from it under any provision of law that I can conceive of being drawn.

Senator THOMAS. It is arbitrary and artificial, and must be.

Mr. REED. Of course, Senators, the provision in the present law for the valuation in 1914 minimizes that effect. I have seen case after case where all this has taken place since 1913 or 1914—

Senator TOWNSEND. How are you going to reach that class?

Mr. REED. On a war-profits basis, with the power vested in the Treasury to make corrections of recognized business factors in each particular case.

I may say this—I just jump from one general proposition to another here, because my time is limited. You wish to tax the excess over a normal profit. You can go to any bank, and they will give you a decision, not necessarily an absolutely mathematically correct decision, but they will give you a decision as to what is a normal income of a normal customer of theirs. It is a business factor. You go to three banks and you get three decisions, and it is a fair result. In other words, what is the normal in any business may be determined by banks on business factors. Congress can prescribe one general factor of prewar profits which will deal with a generality of cases. It can not prescribe all the exceptional factors unless it knows all the special factors in all the business of the country, but it can point out the major general factors that shall be considered in making adjustments and leave the power to make adjustments in the public and as a matter of public record to the Treasurer on business principles by a business board.

We think that it is not necessary perhaps to put in all the odd provisions contained in the English law, but it is necessary to reach

the same result, and it is also, I think, necessary, because of the considerations I mentioned, to give the Treasury power to find that prewar earnings are abnormally high as well as abnormally low and to make an adjustment.

The best general proposition that has been made on that is the Treasury proposition of a graduated 7 to 12 per cent on present capital, graduated for different classes of business.

Senator THOMAS. Why consider capital at all in the matter of a war-profits tax?

Senator SMOOT. You do not have to.

Senator THOMAS. My understanding is that the English law takes the amount of profit in normal years without regard to capital, and then the amounts similarly in taxable years, so that the tax is levied upon the amount of the profit without regard to any question of percentage.

Mr. REED. No, Senator; that is the primary principle of the English law, but it does provide that the taxing power could, at its own election, have a 6 per cent reduction of capital. If it was below that in the prewar year—

Senator SMOOT. But that is only on the business which he started since the war.

Mr. REED. That is true.

Senator THOMAS. Exceptional instances, of course, may exist.

Senator SMOOT. All abnormal profits before the war?

Mr. REED. Yes, sir.

Senator SMOOT. There are only a few instances, relatively speaking, of that kind, and the English law cuts out 95 per cent of that trouble, and it deals directly with war profits, and that is, in my opinion, what we ought to do.

Mr. REED. It gives the capital percentage as a second alternative, and then, aside from the general distinction, it finally gives the Government another alternative that in its judgment the board may base the percentage standard on some factor other than capital. It gives it a practically wide-open door to take some other factor. We had mentioned it last summer and discussed it more and more during the year, and other interests have raised the factor of the ratio of net income to gross income. That is a very leading factor to take into consideration—not to be prescribed by Congress, Senator, but as one of the factors that may be considered by the Treasury.

Senator SMOOT. If you ever go into that there will be another question involved that will be impossible of fair administration to all concerned.

Mr. REED. I judge that none of us have ever thought that out enough to ask it as a final proposition, but still it might be one of the factors to consider.

The CHAIRMAN. Mr. Reed, your time is up. Let me ask you one or two questions before you take your seat.

Do I understand you as approving broadly the imposition in this bill of the war profits tax?

Mr. REED. As now proposed?

The CHAIRMAN. Yes.

Mr. REED. As against the capital percentage tax, yes, sir; not otherwise.

The CHAIRMAN. Do I understand you as opposing the alternative method?

Mr. REED. Unless a capital percentage is levied at the present rates which would make it relatively negligible; yes, sir.

Senator SMOOT. That would hardly be right.

The CHAIRMAN. Then I understand that you either approve or disapprove the arrangement in the bill as to the alternative tax?

Mr. REED. We disapprove very decidedly the increase in rates. We prefer to see that basis entirely out of the law.

The CHAIRMAN. The rates on the war profits tax, or the excess profits tax?

Mr. REED. The excess.

The CHAIRMAN. You do approve of the rate of the war profits tax?

Mr. REED. We approve of the rate of the war profits tax. We disapprove placing the 10 per cent capital deduction on the war profits tax on invested capital.

Senator SMOOT. And I think that ought to be done.

Mr. REED. It ought to be on capital employed; and if it is left in there it ought to be on a graduated scale applying on different businesses. What you lose on one you get on another. That is true of all this.

Senator THOMAS. Your position as counsel for your association requires you to be more or less familiar with taxing systems throughout the country, does it not?

Mr. REED. I beg your pardon?

Senator THOMAS. I say, the position you occupy as legal adviser for a very important organization requires you to familiarize yourself, to some degree, with the taxing systems of the country?

Mr. REED. Yes, sir; it does.

Senator THOMAS. Do you know of a taxing system in the United States, anywhere, that invests the taxing power with an alternate method of assessment and levying.

Mr. REED. I never heard of it, Senator; but I am told that the State of Wisconsin does, in an indirect way, through the operation of its taxes; but I can not see that it is any more effective than, for instance, the provision that the tax shall be on war profits, but shall not exceed 10 per cent—

Senator SMOOT. There is no such provision as that.

Mr. REED. It is not an alternative system; it is a limitation.

Senator SMOOT. We do not provide that at all.

Mr. REED. No; but the alternative simply means that you will take two things, whichever is higher.

Senator THOMAS. The Government can find out which system can get the most blood out of the turnip and then levy it. If we can enact the two methods, why can we not enact half a dozen different methods?

Mr. REED. You could.

Senator SMOOT. You can.

Mr. REED. Whichever is higher or whichever is less.

Senator THOMAS. I would like, if you have time to do so, to make some legal investigation of the subject. I am too busy to make it myself, but I think it is a fundamental question in this bill.

Mr. REED. If I have time after Thursday, Senator, I will take that up.

Senator PENROSE. I would like to address an inquiry to Mr. Reed. He may have covered the point, because I was called out several times.

This committee had a pure war-tax provision up last summer in the revenue bill, but the members of the committee found it almost impossible to meet the argument that many very large concerns would escape taxation altogether as a logical, pure, and simple war-tax proposition. For instance, if I recollect correctly, the Ford automobile concern has no war profits. Would you recommend that that company pay no war taxes, and other concerns of that character?

Mr. REED. No, sir; I would not.

Senator PENROSE. How would you meet that?

Mr. REED. As I pointed out a moment ago, in a great many cases, where you take two apparently equal concerns, one was earning 8 per cent in the prewar period and the other was earning 15. The real value of those concerns, their invested capital, might be nominally the same, but the real value of those concerns in the prewar period was determined by what they were earning in the prewar period, and the consequence is that the one earning 8 per cent was selling at par and the one earning 15 per cent was selling at 150. That corporation is changing ownership all the time. The capital invested in a corporation 30 years ago furnishes no logical, sound, or just basis at all on which to levy a tax against the present owners.

Senator PENROSE. That does not seem to meet my point. We are reluctantly proposing a war-profits tax. Now, assume that at least a half a dozen of the largest concerns in the country, absolutely regardless of any capital or any other way of estimating the tax, have no increase of profits as the result of the war. According to your theory, they would escape any additional taxes?

Mr. REED. No, Senator. I said that we thought that the Government ought to have power to apply some additional factor to those concerns that were earning abnormally high returns in the prewar period as well as those who were earning abnormally low returns.

One general proposition will show what I mean. We were speaking the other day with Judge Hull as to possibilities from this. The capital-stock tax represents capital invested by the present owners—

Senator PENROSE. You are getting back to the excess-profits tax.

Mr. REED. It is simply another basis on which to tax them. In order to make your tax complete, you have to reach these concerns. I understand that on one side of the Treasury they determine the tax on the basis of five or ten millions, and on the other side, with reference to the same corporation—

Senator THOMAS. It is impossible to devise a perfect system of taxation. We can only approach justice and equity. Take such an institution as the Ford concern. If it is taxed, not upon its capital but upon its earnings—and its earnings, we will say, were \$5,000,000 in the normal antewar period, but because of the increase of sales its profits are ten millions in a taxable year, there are five millions which, independent of any question of capital invested, would be subject to this tax.

Senator SMOOT. That is war profits?

Senator THOMAS. Of course, the increase in the income tax is supposed to operate uniformly everywhere.

Mr. REED. Of course, you could put surtaxes on the income tax—

Senator SMOOT. Of course, you get the income tax on whatever is declared in dividends. The Ford income, since the war—that is, the Ford Co.'s profits since the war—have not been as great as they were before the war.

Senator THOMAS. My information is to the contrary.

Senator SMOOT. I have a statement of every year.

Senator THOMAS. Then you have definite information. My information is that as compared with 1911, 1912, 1913, up to last year, it has been very much larger.

Senator SMOOT. Since the war?

Senator THOMAS. Yes.

Senator SMOOT. Oh, no; it has been less. The Ford Co.'s profits have been less since the war than before.

Senator McCUMBER. What objection have you to the present system, 7 and 9 per cent, as meeting those cases of abnormally low earnings before the war and preventing anyone claiming more than 9 per cent investment as a fair prewar earning and taxing as excess profits everything above that?

Mr. REED. I should say the chief objection is that it throws it over to invested capital and the capital percentage basis as the general basis of your tax. The war-profits tax is fairly, as a general basis, resorting to the capital percentage only as one factor in taking care of special cases.

Senator McCUMBER. How would you remedy that?

Mr. REED. I would think the war-profits tax, with the capital percentage feature as the English have it—where it is not equal to 7 per cent of the capital employed—

Senator SMOOT. They have raised it to 9.

Mr. REED. They have raised it to 9—and 9 is fairer.

Senator McCUMBER. How about those who have had an abnormally high earning during the prewar period?

Mr. REED. I would certainly give the Treasury power to find that their earnings had been abnormally high.

Senator JONES. Mr. Reed, what have you to say to the suggestion that you give the Treasury Department the right to fix a normal reasonable profit for each line of business, and then levy the taxes on the excess; in other words, carrying out with reference to prewar conditions the idea that one business ought to earn in normal times more than another business, depending upon the hazard involved in the business? Why not accept that and give to the Treasury Department the right to ascertain what would be a reasonable return upon a given business, and then levy the tax upon the excess, and in that way make quite a variation between the businesses of the country, depending upon the risk involved?

Mr. REED. That is what absolutely has to be done if you are going to get an 80 per cent tax out of every person that you ought to get it out of without substantial injury to any large class. Under any arbitrary system what you take from one man you give to another. You have immunity and confiscation walking together, hand in hand, all the time.

Senator JONES. The House bill, as I understand it, gives a blanket exemption of 10 per cent, and that strikes me as being unfair. There are some businesses which in normal times would be glad to get 6 or 7 per cent, because they get it regularly. There is no risk involved. It is a sure thing, and they are satisfied with it. But other businesses must make a much greater profit in order to take care of the risk of failure in certain years and the risk in the nature of the business itself all the time.

Mr. REED. There are different risks in different classes of business, and a thing that is very often lost sight of is that there are different risks in individual businesses of the same class. A couple of young men go into a mercantile business and borrow all their capital. What they have is very much at risk. They may lose it all, while the merchant around the corner owns it all and there is very little risk.

So there must be power, aside from the power to provide for an earning rate in different classes of business—there must be power to make adjustments to particular businesses, especially if you have borrowed the money, because that is where the biggest risks fall.

Senator JONES. Mr. Reed, are you going to print any part of your remarks that you have not delivered? Because I confess that I do not fully understand your argument, but I am not going to take up any more of the time of the committee with any further inquiries.

Mr. REED. I shall do that, and will furnish copies to the members.

The CHAIRMAN. I wanted to ask a few questions.

I understand you to be objecting to the basis of ascertaining the amount of capital applying the deductions upon that capital. As I understand the House bill, if the deduction is to be estimated according to the war profits method, the amount of deduction allowed is 10 per cent on the invested capital.

In the case of the excess-profits tax methods, the amount of deduction allowed is 8 per cent of the excess profits.

You think that is not quite a fair method of ascertaining the deduction?

Mr. REED. I think that the definition of invested capital, throwing it back to the original investment of 30 years ago, is absolutely unsound and unfair—

The CHAIRMAN. You do not approve of that. But eliminating this method of ascertaining the deduction, do you approve of the rates provided as to war profits and excess profits? Do you think the rates are properly and equitably adjusted in both of those methods?

Mr. REED. Speaking for a client, having no definite instructions. I received no objections from any interests to the rates as such. Our objection to the capital percentage tax is really based upon our objection to that basis of tax.

The CHAIRMAN. You have no objection to make to the adjustment of rates between those two methods?

Mr. REED. I make no objection or protest against the rates as to the war-profits tax, the rate as such; but the injustices, the necessarily unavoidable injustices and hardships under the capital percentage basis are so great that if we must have it the country can not stand it.

The CHAIRMAN. Your objection, then, goes to the method of ascertaining the invested capital——

Mr. REED. Yes, sir; and to the capital percentage basis generally.

The CHAIRMAN. Now, I understand you as taking the position—and that I think is the most important matter that you have brought out—that the bill ought to prescribe the tax that is to be paid by the man whose income is normal and whose income can easily be ascertained by a process of calculation, but you think there is a large number of exceptional cases where the income can not be easily ascertained, where the amount of capital invested can not be easily ascertained; and in that class of cases you think we ought to invest the Secretary of the Treasury with broad powers to ascertain what the invested capital is and what the proper rate of interest is?

Mr. REED. I think that is absolutely essential if you are going to get an 80 per cent tax and get it where it is to be had from those who really have the excess profits.

The CHAIRMAN. In other words, to set up a kind of exceptional case in this bill and to permit the Secretary of the Treasury in that exceptional case to ascertain the invested capital and to assess the income in his judgment and discretion?

Mr. REED. To ascertain the normal income.

The CHAIRMAN. Taking into consideration all the circumstances and conditions in each exceptional case?

Mr. REED. Yes, sir; that is the most important thing.

Senator GERRY. In other words, you make an exception in that case the same as you do in the exceptional case in the prewar case?

Mr. REED. Yes, sir; I would.

I do not question the constitutionality of it, because I believe that constitutional questions must be determined on broad general lines. If you have power to levy a war tax on the excess above the normal income, there is only one way in which you can do it, and that is to have the normal income determined and fixed, because it can not be prescribed by statute.

The CHAIRMAN. If it is a normal case, under the process of assessing this income tax provided in the bill, probably no great injustice would be done as between businesses and as between persons subject to this tax.

Mr. REED. I would only say that as to war profits taxes; not as to capital percentage taxes.

The CHAIRMAN. But no great injustice would be done as between the taxpayers, no great discrimination as between the taxpayers by the application of these two methods to the normal case. The injustice will come by its application to the abnormal case; and to avoid that possible injustice you propose this exceptional case with power in the Secretary of the Treasury to adjust equities?

Mr. REED. I should say very decidedly that in my judgment the capital percentage tax with increased rates rests unjustly in the normal case.

Senator SMOOT. Without doubt.

Mr. REED. And destroys the values that have been invested in stock and securities in the last 5 or 10 years.

The CHAIRMAN. You reach that conclusion because you think the time for assessing the value of the property which constitutes the capital is the wrong time?

Mr. REED. It is the wrong time. The property, in many cases, is assessed on the assessment made by other parties 30 years ago, with no relation to the investment made by the present owners in the last few years.

The CHAIRMAN. Instead of the invested capital being ascertained by valuing the assets at the time of their acquisition, you insist that the assets ought to be valued as of the date the tax is levied?

Mr. REED. That can not be done, of course, Senator.

The CHAIRMAN. As of the date the bill passes?

Mr. REED. I am opposing the capital percentage basis. You have got to value that property as nearly as you can as to the value placed upon it the preceding year—

The CHAIRMAN. In other words, for this year you would think you should value the assets as of the 1st of July, 1917?

Mr. REED. That would be a decided relief and work justice in a great many cases.

The CHAIRMAN. Now, Mr. Reed, if that were done, if we were to ascertain now the invested capital for the purpose of applying this 8 or 10 per cent, as the case may be, as of the 30th day of June, 1917, do you not think by reason of the greatly inflated value on that date, under those rates, we would get a very small tax, relatively speaking, and that in order to get the amount that we are seeking to get from incomes and profits, that we would have to enormously increase these rates?

Mr. REED. An 80 per cent tax is a pretty heavy rate, Senator.

I would like to answer, if I may, by an illustration of a case that came to me. A man had invested some three or four hundred thousand dollars—

The CHAIRMAN. Just let me finish, now. For instance, take for illustration this: Suppose you have a steamboat company which owns half a dozen big vessels of the larger type, we will say. If you are going to value those vessels, which are that company's assets, if you are going to value them at the price they would have brought on June 30, 1917, their capitalization is perfectly enormous.

Mr. REED. No more enormous, Senator, than the man who bought them at that price at that time—

The CHAIRMAN. Ten per cent of their capital stock would wipe out very largely their net income, and there would be nothing left to tax.

If you are going to take mines, coal mines and iron mines, and value them for the purpose of this deduction at the enormous price at which they would sell now, would you not have a capitalization that would be so much that the 10 per cent upon it would wipe out very largely the profit and we would get no tax from these incomes, or if we got some, it would be relatively a very small tax?

Mr. REED. I did not intend to find myself arguing as a direct proposition for a valuation in 1917—

The CHAIRMAN. That is what you have been arguing.

Mr. REED. No; I have been arguing against the capital percentage basis, because it is unfair.

Senator SMOOT. Entirely.

Mr. REED. As long as you ask me, I will say this, Senator, that logically and fairly, with this enormous tax, honestly that is what you should do, and I will answer it with an illustration. It is a tax on the profits of 1917 or 1918, as the case may be.

In the case I was going to mention a moment ago, a man invested \$400,000 back in 1914, I think, or 1913, in the development of some new process for extracting gasoline, I think, from the oil fields. He bought up contracts at nominal prices. Incidentally, he had spent so many thousands of dollars before that in other forms in experimenting with that process, but he had only \$400,000 invested in 1917. Those contracts he had obtained at low figures, and he was offered for that business two and one-half millions. I can not quite get it out of my own head that that man was worth two and a half millions at the end of 1916, just as much as the man would have been who paid him two and a half millions for it.

Senator SMOOT. Of course, under that plan we would not collect any taxes.

I am speaking of the general business of the country. The trouble with an excess profits tax and the trouble with a question of valuation of stock or capital, which is virtually the same thing, is that it is impossible to put into operation.

Senator THOMAS. I think the illustration of the chairman shows that.

Mr. REED. With that kind of a valuation, Senator, you would not have to have so high a percentage deduction. That is high because you know it is unjust in many cases. Even in the English law, Senator, the law values the present property at its cost, which is a very different thing from valuing the investment 30 years ago. It is much fairer.

Senator SMOOT. Quite true.

Mr. REED. In fact I think that would be a very decided advance over the present bill if that were done.

The CHAIRMAN. I have been asked to state that Mr. H. C. Brent, of the Fidelity Trust Co. of Kansas City, has been asked to appear here for the Kansas League of Municipalities in protest against the direct tax against municipal issues and also against the tax I have mentioned, and that he has telegrams from a number of cities—Atchison, Kansas City, and others.

He would like to take three or four minutes to present those protests.

The CHAIRMAN. He wishes to appear for the bondholders?

Mr. REED. No, sir; the Kansas League of Municipalities, Mr. Gwinn, the city treasurer of Baltimore, is present, and would like to address you briefly.

The CHAIRMAN. For the purpose of discussing the tax on municipal bonds?

Mr. REED. Yes. Those are the only two.

The CHAIRMAN. How long do those gentlemen desire?

Mr. REED. About three minutes each, I believe. That also includes Mr. Gwinn. Mr. Chairman, before I finish I desire to present a brief in the form of a memorandum which I wish to be made a part of my remarks.

(The memorandum referred to above is as follows:)

OUTLINE OF POINTS—EXCESS AND WAR PROFITS TAX.

A. ANALYSIS AND CRITICISMS OF HOUSE BILL.

1. Definition of invested capital changed from present law.
 - (a) 1914 valuation of tangible property omitted.
 - (b) "Paid in surplus" on tangible property omitted.
 - (c) Illustrations.
2. Principle of invested capital unsound.
 - (a) Tax is on excess profits of present stockholders whose capital is invested in stock at values of present properties in recent years.
 - (b) No necessary relation in fact between original investment and properties.
 - (c) 80 per cent tax on excess above 10 per cent of original capital may actually (on one hand) be 80 per cent tax on excess above 2 per cent of investment of present owners or (on other hand) leave a 20 per cent of such investment untaxed.
 - (d) Gives relative immunity to watered capital and penalizes conservative capitalization.
3. No general or adequate power to deal with exceptional cases.
 - (a) Sec. 327 limited to specific classes.
 - (b) Simply applies a secondary arbitrary basis of tax.
 - (c) This basis unsound and probably unconstitutional.
 - (d) Measures C's tax by income of A and B.
4. Prohibition of consolidated returns invites evasion of tax. (See 336.)

B. PROPOSALS.

1. War-profits tax, alternative or exclusive, should reach all profits above normal during the war year.
 - (a) Normal profit determined prima facie by prewar standard.
 - (b) Adjusted in exceptional cases.
 - (c) What is normal profit in given case is business question which can be decided by administrative officer or board analogy to valuation of property by local assessors.
 - (d) Principle to be recognized one of taxation, not of profits limitation.
 - (e) It is constitutional and practical and also essential.
2. Capital (when used) should be present assets.
 - (a) Determined by balance sheet adjusted to meet statute.
 - (b) Valuation should exclude appreciation due to war conditions except where property has been acquired at appreciated value. Some allowance for purchase of stock representing appreciation should be permitted in exceptional cases of hardship and also where appreciation has been capitalized and taxed to stockholders.
 - (c) English valuation is cost or value when acquired, less depreciation; and indebtedness is deducted.
 - (d) 1914 valuation should be allowed in any event to minimize inequalities.

The House bill changes the present excess-profits tax in two vital respects. First, the rate of tax is made confiscatory of the so-called excess profits, and, second, although the House committee's report states in terms that the "definition of invested capital in the existing law . . . has not been changed in any important particular," it has in fact been changed in its most important particular, that of the valuation of tangible property acquired for stock. Under the present law and regulations tangible property acquired for stock prior to January 1, 1914, is required to be valued as of that date, and any excess over the par value of the stock may be allowed as "paid-in surplus" (Regulations No. 41, art. 63), while under the pending House bill, section 320, there is allowed only "actual cash value of tangible property, other than cash, bona fide paid in for stock or shares at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor."

The following illustrations of the operation of this provision with the greatly increased rates of tax speak for themselves:

1. A Co. was formed in 1905 and \$10,000,000 stock was issued for properties which at that time were earning \$800,000 and (probably) could have been

bought for \$4,000,000. Between 1905 and 1912 the company's earnings were high and it put \$700,000 into surplus. Its average prewar net income was \$900,000 and its stock was selling in 1914 on a valuation of \$6,000,000. By 1918 its surplus had increased to \$1,400,000. It is now earning \$1,200,000. It values the original property at \$10,000,000 on its excess profits return and puts its invested capital at \$11,400,000. The Treasury can obtain no proof of actual values in 1905 except that shown on the company's books and supported by the subsequent earnings. On a war-profits basis it would be taxed 80 per cent on \$300,000, its excess over \$900,000, a tax of \$240,000. By the 10 per cent limitation based on invested capital, its misnamed "war-profits" tax is limited to 80 per cent of \$60,000, the excess over \$1,140,000, a tax of \$80,000, a loss to the Government of \$192,000. The actual tax under the graduated rates would be 35 per cent of \$288,000, the excess over \$912,000 (8 per cent of \$1,140,000), a tax of \$110,800, a net loss to the Treasury of \$129,200. Its real, original invested value was \$5,400,000, on which it is earning over 22 per cent and enjoying immunity up to 17 per cent (\$912,000).

2. B Co. was formed by K. and L. in 1905 with \$2,000,000 stock. They turned over to it for the stock a family partnership business for which the partners had just refused a cash offer of \$5,000,000. They appraised the physical properties at \$3,500,000, but thought that \$1,000,000 each was enough stock. They had no reason except personal conservatism for undervaluing the properties. They have kept up the properties, but paid out their net earnings and would have under the House bill a present invested capital of just \$2,000,000. In 1914 they refused \$7,000,000 for the property. They have averaged \$400,000 a year on the property since 1905, this also being their average prewar net income, and are in 1918 trying to avoid profiteering and doing necessary war work with a net income of \$470,000. They are taxed under the 80 per cent over 10 per cent clause on the excess over \$200,000, which is 4 per cent of the price they refused for the property in 1905, less than 3 per cent of what it was worth in 1916, a total tax of \$216,000, leaving them (subject to corporation income and personal taxes) \$254,000.

Incidentally K. died in 1916, leaving his widow only a one-twentieth interest in his share, valued for inheritance tax at \$159,000, and producing an income of \$10,000 a year. Or possibly he has sold a one-fortieth interest or 250 shares to J. for \$300 a share, paying an income of \$5,000 a year. In either case the income is practically cut in half. All parties concerned will probably sell out the company to new owners who on a new valuation are relatively untaxed. A company in the position of A Co. (Illustration 1) or E Co. (Illustration 5) could take it over without incurring any additional taxation.

3. Corporation C was formed in 1915 by new parties and acquired the properties of either corporation A or corporation B, either for cash or stock, at a valuation, say, of \$7,000,000. In either case they have an invested capital based on the actual 1915 valuation plus their surplus since 1915, say, \$300,000. Earning \$1,000,000 net (the same as A Company) they will be taxed 80 per cent on \$470,000 (excess over \$730,000) or \$376,000. On an earning of \$470,000 (same as company B) they would not be taxed at all.

In each case the comparison of the recently formed company having a prewar valuation with a company formed in earlier years is very striking.

4. D Company was formed in 1900 by M. and N. on an investment of \$100,000. Its properties have been kept up and developed and have appreciated greatly in value, but it has not an "earned surplus." O. and P. bought the company from M. and N. in 1914 for \$500,000, paying that price for the stock. The company is taxed on its excess over \$8,000 or \$10,000; that is to say, 8 per cent, or 10 per cent on its invested capital. O. and P., its owners, are taxed on the excess over 1½ per cent, or 2 per cent of their investment.

5. M. and N. formed corporation E in 1900 with investment of \$1,000,000. The properties have been kept up, but the company's earning power has been poor and the actual value of the property had depreciated in 1914, when the stock was bought by O. and P. for \$500,000. In this case O. and P. have immunity from tax up to 16 per cent, or 20 per cent of their investment.

6. Restating 4 and 5, O. and P. in 1914 bought two corporations for each of which they paid \$500,000. The properties were substantially equivalent in value and earning power, and one, to all intents and appearances, was the same as the other. In 1918 they are told that 80 per cent of the excess of the profits of D Company over \$10,000 and 80 per cent of the excess of the profits of E Company over \$100,000 are to be taken in tax—in the one case 2 per cent of their

investment, in the other 20 per cent is the "war-profits" credit. They ask for a reason for the very wide divergence and are told that it is because M. and N. only put \$100,000 in B Company, while they put \$1,000,000 in E Company. They ask if there is any other reason, and the reply is none.

None of the cases cited above are in character exceptional (except perhaps that of C Company, though some of them may be more extreme than the average case). Company A is typical of the watered stock companies; Company B of the undercapitalized companies; and Company C of newly formed companies; while O. and P. are typical of the great body of stockholders who have invested their capital in corporate enterprises at actual values and who will be taxed under this bill according to the accident of the original investment and not in any way according to the present or even prewar value of the actual properties which they acquired by their purchase of stock. A great many concerns whose values a few years ago were and now are in fact far below the original investment are practically immune from tax, while stockholders who have paid for the appreciated values of successful developments, will find their income, whether large or small, confiscated. The point is that there is no necessary relation in fact between the original investment of the original promoter and the values and actual investments of the present stockholders. It is the present stockholder and not the original promoters who are taxed. No such unsound and accidental foundation can support an 80 per cent tax.

Under the bill, the Government would practically confiscate the income of one class of stockholders and then with equal lack of intent given to the other class what it has taken unjustly from the first class. Although no figures are available it is believed, that, especially in the immunity given to watered-stock concerns and to concerns whose original values have appreciated, the Government would lose as much as it took unjustly from the other class of stockholders. By using a fair basis the Government, we believe, can get an equal amount of revenue. Certainly if the basis is fair it can and will get all that it can safely take from the business profits of the corporations of the country.

We very respectfully urge that the 1914 valuation provision of the present law be retained, and that in any event where the taxpayer can prove an actual value paid in in excess of the stock issued, such value be allowed as "paid-in surplus," which in fact it is. The suggestion has been made that one reason for refusing to allow "paid-in surplus" in this case is that the stockholders may have undervalued their property for the purpose of keeping down the State organization tax. Assuming this to be so in some cases—and this is we believe permitted by the laws of most States—we are sure that so small a consideration could not be taken by the members of your committee to justify so punitive and unjust a penalty or undercapitalized concerns. It would be very much like shooting a soldier on learning that he had stolen jam from his grandmother as a small boy. The discrimination which the bill makes in favor of overcapitalized concerns is a much more serious matter, and the proposed confiscatory profits tax on the excess over fixed percentages of "invested capital" as defined in the bill is so serious that it would be difficult to overestimate its effect, if enacted, at this very critical time.

2. *Principle of invested capital unsound.*—There are also, of course, serious objections to the principle of invested capital and to the allowance of original cash investment where the original property has disappeared or become valueless and new property has taken its place. The present properties represent the investment of the present stockholders, and assuming that inflated war values are to be avoided and that some adjustment is necessary to meet prevailing views as to this our suggestion would be that the capital be taken to be the present assets at cost or value when acquired, or if acquired prior to 1914 at their value on January 1, 1914. Borrowed money or indebtedness could, of course, be deducted, if this is desired, and the corporation balance sheet adjusted to meet the law would form the basis of the capital determination. This would accord substantially with the English law, except as to the 1914 valuation.

The 1914 valuation substantially minimizes the evil inherent in the principle of "invested capital." With this allowance—and without any limitation by the par value of the stock—prewar concerns are put on a generally equal basis. And there is no express advantage given to watered capital. We expect to urge the English plan of the valuation of present assets as opposed to that of original investment (but with some allowances for appreciation), the capital percentage standard applying, of course, only to new businesses and new capital and as a limitation on the war-profits standard.

3. *No general or adequate power to deal with exceptional cases.*—We do not wish to minimize the relief which can be given in some cases under the so-called representative basis, popularly known as section 210 under the present law. Taxpayers, we know, have been glad in many cases to avail themselves of it while they laughed at its artifice. The truth is, of course, that there are no absolutely representative concerns from which to get a rate of earning for a single year. Such earnings are never uniform. If corporations B and C combined earn \$100,000 on \$600,000 capital in 1918, then A is conclusively presumed to be earning \$30,000 on \$180,000, although the actual figures are apt to be as follows: B earns \$30,000 on \$250,000; C earns \$70,000 on \$350,000; A earns \$30,000 on \$100,000.

B does a conservative business on his own capital. C does a moderate business on partly borrowed capital, and A's capital is both borrowed and watered. The point, of course, is that no discretion is intended to be given to the Treasury in terms. Instead of adjusting A's war-profits credit according to its actual factors by comparison with other concerns, we must apply another arbitrary factor prescribed by Congress and tax A on a rate of tax fixed by the earnings of B and C. The Treasury, in fact, has a discretion uncontrolled by any principle, i. e., to pick representative concerns that will as nearly as may be give A a proper tax.

(a) Not being supposed to know A's invested capital, they select or try to select, not concerns representative of a trade as a whole, but concerns which will in fact give them a fair tax as to A.

(b) They must find not a war-profits deduction, but a rate of invested capital to net income. This ratio itself controls the rate or percentage of the tax on the income. For instance, in the case cited above the net income is 16½ per cent of the invested capital, and all concerns to which this is applied are subject to a tax of 5¼ per cent (80 per cent of 16½ per cent, minus 10 per cent) of the assumed invested capital, or 32 per cent of the actual net income.

(c) We do not pretend to know how strictly the department follows the letter of the law, but we judge that a fair selection of candy stores, shoe factories, and cotton mills would furnish a rate of tax suitable to a number of watered stock industrial combines. That is about all the principle we can find in this proposition.

In our judgment this practically discretionary power to apply an artificial basis of tax is unsound and tends to weaken and discredit the administration of the tax.

4. *Prohibition of consolidated returns.*—It is a well-known fact—we are sure the Treasury records will bear us out—that the separate net incomes of different corporate units used in a single enterprise are wholly arbitrary and reflect not the actual earning power of each unit, but the amounts which for convenience or otherwise are allowed to be credited to them. For instance, we have a manufacturing plant worth, we will say, \$1,000,000, owned by company A and rented to company B for \$80,000 a year, earning 8 per cent net on its capital. Company B is an operating company with nominal capital and would fall under section 203 of the House bill and pay only 20 per cent on its net income. It operates A's plant at a profit of \$150,000 a year. On a consolidated return the invested capital would be \$1,000,000 and the net income \$230,000, and the tax would be 35 to 70 per cent on the excess over 8 per cent, about \$79,500, or possibly 80 per cent on the excess over the "war-profits credit," as the case might be. By the separate returns required by this bill A would pay nothing; B would pay 20 per cent on the \$150,000, or \$30,000, a loss to the Treasury in this relatively small case of at least \$50,000.

It is evident, of course, that the diversion of income from one controlled unit to another is almost entirely in the control of the taxpayer.

PROPOSALS.

1. *War-profits tax should reach all taxpayers.*—We do not accept the view that the "war-profits tax" can not be made to reach all taxpayers. We have no doubt of the wisdom or practicability of such a tax. The difficulty seems to be to secure a legislative recognition of the broad administrative power essential to the idea of a confiscatory tax on excess profits. This year, as last year, the bill, to use the hackneyed phrase, camouflages the discretionary power actually given, and in the exercise of this power compels resort to artifices and

subterfuges to mitigate the injustices of the prescribed rule. So far as any constitutional principle is involved, the practical arbitrary and irresponsible power to select representative concerns and compute a rate of tax from such concerns is much more questionable than would be a direct mandate to determine (what is actually desired) the fact as to a normal return from the capital and other factors employed in the given business. Any banker could give a decision as to whether or not a given customer is making a normal profit in his business. Two or more bankers might differ on the figure, but an actual decision could be had, and the average of three business opinions would be fair, just as fair and correct and quasi judicial as the valuation placed by a local board on a piece of real estate for taxation purposes, and much fairer than a representative rate of tax based on the false assumption that a corporation's net income on its capital in a given year actually approximates the ratio established by two or more of its competitors.

The English law proceeds, we take it, on this principle. We are confronted with a somewhat different situation, but with the same great emergency of war. The executive branch is charged primarily with the duty of winning the war. The autocratic powers already given it for this purpose are immeasurably greater than the power now proposed, to determine according to the legislative standard the war profits which must be taxed for war purposes.

As a tentative draft, solely to illustrate our proposal, we submit the following as a subdivision of section 312 of the House bill:

WAR-PROFITS TAX—POWER TO DEAL WITH EXCEPTIONAL CASES.

(Tentative draft.)

SEC. 312. (d) In any case where the Commissioner of Internal Revenue, under rules and regulations approved by the Secretary of the Treasury, shall determine that the war-profits credit computed under subdivision (a) does not represent a normal profit per unit of business or a normal return on the capital and other factors employed in such trade or business, either because the factors included or excluded in the computation of net income of the taxable year, or because by comparison with representative concerns in like or allied businesses or industries the profits per unit of business or the net income of the prewar period was abnormally high or relatively low, or because of any other similar circumstance, the commissioner, subject to such rules and regulations, shall make such proper modification of the war-profits credit as may be necessary to make the computation thereof correspond to the computation of net income for the taxable year and, as nearly as may be, equal to a normal profit per unit of business and a normal return on the capital and other factors, if any, employed in producing such income; and for such purposes the commissioner shall compare the taxpayer with representative concerns whose war-profits credit has been satisfactorily determined under this title and which are, as nearly as may be, similarly circumstanced with respect to units of business, to capital and other income-producing factors, and to all other relevant facts and circumstances: *Provided*, That in no case shall such war-profits credit be less than — per centum ("or the general trade percentage" proposed by the Treasury) of the capital employed. The capital employed, so far as it does not consist of money, shall be taken to be (a) the value on January first, nineteen hundred and fourteen, of all assets acquired prior to said date, (b) the cost or value when acquired of all assets acquired on or since January first, nineteen hundred and fourteen, and (c) the face value of all debts due which have not been allowed as worthless and deducted from gross income for income-tax purposes, less (1) any depreciation in any assets included under (a) or (b) due to wear and tear or obsolescence, and (2) any unpaid purchase money or other indebtedness. Any appreciation in the value of any asset over the cost thereof occurring since January first, nineteen hundred and fourteen, may be allowed only if and to the extent that the amount thereof has in or prior to the taxable year been carried to capital account and credited to the stockholders by way of a stock dividend or has otherwise directly or indirectly become chargeable to the stockholders as a profit or income for the purpose of taxation.

The CHAIRMAN. Mr. Brent, we will hear you now. You are speaking for the investment banks?

STATEMENT OF MR. H. C. BRENT.

Mr. BRENT. For the Bankers Association. I am here not so much to discuss the merits of the bill, because it was only recently brought to my attention——

Senator PENROSE. Whom do you represent?

Mr. BRENT. These telegrams have come to me from various municipalities in the western territory.

Senator PENROSE. Do you officially represent those cities? Have you been designated by them and officially selected by them to represent them?

Mr. BRENT. I think if I read one of these telegrams it will answer your question.

Senator PENROSE. Well, I just make the inquiry.

Mr. BRENT. This is addressed to me here——

The CHAIRMAN. You need not read the telegram. You say you are authorized to speak?

Mr. BRENT. Yes, sir.

This is from the League of Kansas Municipalities, from Homer Talbot, secretary, Lawrence, Kans.——

Senator SMOOT. Just put the telegrams in the record:

(The telegrams referred to are here printed in full, as follows:)

KANSAS CITY, KANS., September 8, 1918.

H. C. BRENT,

*Care H. C. Flower, Metropolitan Bank Building,
Washington, D. C.:*

Will you please represent League of Kansas Municipalities, composed of 134 cities and towns, before Senate committee to-morrow morning in protest against direct and indirect taxes on municipal bonds included in income-tax section of House Ways and Means Committee revenue bill.

LEAGUE OF KANSAS MUNICIPALITIES,
HOMER TALBOT,
Secretary, Lawrence, Kans.

LAWRENCE, KANS., September 9, 1918.

H. C. BRENT,

*Care H. C. Flower, Metropolitan Bank Building,
Washington, D. C.:*

Kindly represent city of Lawrence before committee and protest for us against any direct or indirect tax upon municipal bonds. Such action would cripple the functions of municipal government, and the gain Government would receive could not possibly offset injury of such tax. Municipal borrowings are at minimum now and Capital Issues Committee has sufficient authority for control.

GEO. L. KREECK,
Mayor of Lawrence.

KANSAS CITY, KANS., September 9, 1918.

H. C. BRENT,

*Care H. C. Flower, Metropolitan Bank Building,
Washington, D. C.:*

Want you to appear for Kansas City before Ways and Means Committee Tuesday morning and protest against any direct or indirect taxes on State and municipal bonds.

H. W. MENDENHALL, Mayor.

INDEPENDENCE, KANS., September 9, 1918.

H. C. BRENT,

Care H. C. Flower, Metropolitan Bank Building, Washington, C. C.

Please enter protest against a direct or indirect tax on municipal bonds included in income section of House Ways and Means Committee revenue bill.

CITIZENS FIRST NATIONAL BANK.

KANSAS CITY, Mo., September 9, 1918.

H. C. BRENT,

Care H. C. Flower, Metropolitan Bank Building, Washington, C. C.

Will you be kind enough to represent the city of Atchison, Kans., before Senate committee to-morrow morning in protest against direct and indirect taxes and municipal bonds included in income-tax section of House Ways and Means Committee revenue bill.

VICTOR L. KING,

City Clerk of Atchison, Kans.

Mr. BRENT. The point that they seem to think is the most interesting to them is whether or not, by levying this tax, the Government would get a revenue commensurate with the charge they place upon the municipalities themselves. This tax will of course necessitate their floating their bonds at a higher rate of interest. The tax will last during the war and possibly a few years afterward. The charge on the municipality will last from 25 years up; and I just want to ask you gentlemen to consider that. I have never figured it out, but I must say that it is well worth consideration.

Senator THOMAS. If we can tax a municipal bond we can tax a State bond, I think. If we can tax revenue from a State bond, why can we not tax revenue from the State directly? Logically, does not the power to tax the bonds of a municipality involve the power on the part of the Government to tax the income of a State direct?

Mr. BRENT. I am not questioning the power of the Congress—

Senator THOMAS. I am. I am questioning it absolutely until I am better informed.

Mr. BRENT. Yes; you are. Some of them so hold, that there is no power in Congress to tax them.

Senator THOMAS. My judgment is that the holders of municipal bonds can make themselves more useful to us by determining not the rate of taxation or its effect upon the municipal bonds; but, fundamentally, the power of one sovereignty to tax the securities of another.

Mr. BRENT. I am not capable. I am not trained or posted or able to argue that question with you, Senator. I have no doubt that this committee, composed as it is, would know more about it than I would. I am simply here to suggest that we feel that the Government, by adding this tax, would not get a revenue commensurate with the charge laid against the various municipalities that will have to pay the added interest.

Thank you, very much.

Mr. REED. Senator Simmons, I intended to join in that request Mr. Gwinn, register of the city of Baltimore, who desires to speak.

The CHAIRMAN. About the same matter?

Mr. REED. Yes, sir. Mr. Brent merely had these telegrams to present.

The CHAIRMAN. Very well. Then I will announce that after hearing Mr. Gwinn, the hearing upon that part of the bill is ended. You may proceed, Mr. Gwinn.

Senator McCUMBER. What is your position, Mr. Gwinn?

**STATEMENT OF MR. RICHARD GWINN, CITY REGISTRAR OF
BALTIMORE, MD.**

Mr. GWINN. I am the city register of Baltimore, the financial officer to take the place of the treasurer. I am the only treasurer that the city has.

I do not want to say very much. What I have to say is altogether on the matter of taxing municipal securities and State securities.

In the committee's report it seems to me that they practically anticipate that there is some doubt as to the constitutionality of it. The only object I can see that the bill is after is to produce some revenue, and as a matter of fact, that part of the bill which taxes the future issues will not produce much revenue, very little; and the retroactive part of it will produce perhaps more. I do not know, but certainly the entire amount of revenue that would be produced under this bill would not be in any proportion even to the danger which the House committee speaks of in its report.

There is one other thing that they might have in view, and that would be—well, they also speak of the unfairness of it—

Senator JONES. Have you tabulated the quantity or the amount of these securities outstanding and the interest return?

Mr. GWINN. No; I have not; but it is not necessary to do that for it to be plain, Senator, that the amount of revenue would be inappreciable as compared with the results; it would be inconsiderable.

As far as the new issues are concerned, they have already been reduced to a minimum, and as has already been stated here, there are no new issues to come out except for absolute necessities, and the most of them are for your own purposes, for the purpose of the Government, indirectly. So that it can with equal reason be assumed that it will be very small. But there is something else to be said, even though the revenue were larger.

So far as the fairness is concerned, it has been also stated here that there is no such thing as fairness, or exact fairness, in taxation. Those who are familiar with any taxation would know that. The unfairness would seem to be as far as taxing new issues is concerned as against the old issues, which are not disturbed except indirectly—but it is not a question of fairness at all. It is not a question of taxation of the holder of these securities, because whilst he is the one that brings the money to the Treasury, the State is the one that is taxed. It is not a question of fairness with the State; it is a question of agreement—agreement with each other in the federation and in the constitution which they have adopted. It is a question of whether or not they have any power to do it.

There is one other point I want to speak of, and that is the possible fear of competition that to my mind seems to be the only reasonable cause for attempting to tax municipal or State bonds or anything coming under that head. As far as competition is concerned, they are not in competition with the former issues. Our liberty loans are not in competition with the former issues at all. If they are, they have been in the past; but the sales and purchases of State and municipal securities have been so small as not to interfere with them

at all. I do not think that anybody can look back and truthfully say that the exempt municipal and State bonds have been in actual or noticeable competition with the liberty bonds. I do not think so.

As far as new issues are concerned, the same argument would apply. Because of the meagerness of them you can take them out of competition, because that would be negligible. The only competition that I can see that the liberty loans would be subjected to would be that competition which this very bill would bring about by imposing a tax and by dislodging all of that stuff which now lies quiet, and it would not be disturbed at all by reason of the liberty loans or by reason of any rate on the liberty loans.

Senator THOMAS. In other words, the effect of the bill would be to produce the very competition which the bill seeks to avoid?

Mr. GWINN. Precisely so. I mention that, not that I have heard it advanced by anyone, either the committee or anyone else, but, nevertheless, it appears to me to be a natural reason why some tax should be put on municipal bonds to keep them out of competition. That sounds very well, but it will not do that.

Senator THOMAS. Does Maryland impose a State income tax?

Mr. GWINN. No, sir.

Senator McCUMBER. You assume that the real purpose of the bill is to prevent competition?

Mr. GWINN. No; I do not quite say that.

Senator McCUMBER. The real purpose is to secure funds; to get taxes?

Mr. GWINN. Yes; I understand that.

Senator McCUMBER. Without reference to the competitive proposition.

Mr. GWINN. That is perfectly true; but, as I say, it does not appear to me that the additional taxes which this bill will bring from the taxing of municipals, in the present form of the bill, will be considerable as compared with the sacrifice or with the dangers which are carried by the threat of its not being constitutional.

There is one other point that occurs to me, and that is the question of interest. If this tax is imposed upon municipals, new issues, the State pays it. The State does not write the interest in the bond that it is going to pay at all. It puts it in there because it is the custom, more or less; but the State pays the interest on that bond in accordance with the basis upon which it is sold, and if the tax goes into the bond the basis changes. It not only will change on municipals, but if the tax is imposed on municipals, then they are in competition with all other issues, industrial and otherwise, and there is no telling where it would go. The United States Government would be in the same position, because it will have to follow along in competition with those things. They will be in greater competition, as I see it, than they would be leaving these undisturbed.

Furthermore, it seems to me to be a great pity to dislodge the last mooring that we have to any kind of stability of rates. It seems to me it would be a great pity to do so.

I thank you. That is all I have to say.

The CHAIRMAN. Senator Smoot suggests that the committee hear Mr. Charles F. Wetzel, representing the National Association of Merchant Tailors, rather than Mr. Cooper, who is next on the list.

because Mr. Wetzel finds it necessary for him to take an early train. How much time will you desire, Mr. Wetzel?

Mr. WETZEL. Oh, a very short time—5 or 10 minutes.

The CHAIRMAN. Very well, proceed.

Let me say that Mr. Cooper, of Virginia, will be heard immediately after we get through, if we have time, before 1 o'clock. Otherwise we will hear him in the afternoon.

STATEMENT OF MR. CHARLES F. WETZEL.

Mr. WETZEL. I have a brief here, Mr. Chairman, addressed to the Finance Committee, United States Senate—

The CHAIRMAN. Would it not answer your purpose as well to have that brief printed and just talk to us and give us in that way what you have to say?

Mr. WETZEL. It is very brief; it is but a few pages. It gives all the details.

The CHAIRMAN. Very well.

Mr. WETZEL (reading):

To the FINANCE COMMITTEE,

United States Senate:

In re proposed tax on clothing: As patriotic citizens we cordially indorse the policy of the Government in its effort to bring this world-wide war to a speedy and successful termination. We acclaim this policy as exemplified in the new draft law. We indorse the intent of the proposed fiscal law now under consideration by your honored committee, and having for its object the raising of \$8,000,000,000 required to arm, clothe, pay, and feed the armies now on the front and being formed here.

We fear, however, that the proposed law as now worded will defeat its object; i. e., the raising of the largest amount of money levied by any government. We refer to the proposed tax on clothing, which we take exception to, as tending to class legislation, and, as proposed, would reduce the amount secured to a negligible figure. All merchant tailors agree that a flat tax of 10 per cent placed on all clothing made would produce results and prove equitable to all concerned. This tax, to be applied on all clothing sold in the United States, whether made here or abroad, as applied would work out as follows: A \$10 suit or overcoat would cost \$11; a suit or overcoat selling for \$100 would cost \$110.

Respectfully submitted.

NATIONAL ASSOCIATION OF MERCHANT TAILORS OF AMERICA.
CHARLES F. WETZEL, *President*.

Supplementary, I have another brief which gives a little more of the statistics of the amount that you would get against the amount that you would receive if all clothing were taxed [reading]:

To the FINANCE COMMITTEE,

United States Senate:

In re proposed tax on clothing: The proposed law of taxing purchasers 20 per cent on suits and overcoats exceeding the price of \$50 will have the final result of abolishing the high-grade merchant-tailoring industry, the consequence of which will throw thousands of men and women out of employment, including coat makers of all descriptions, waistcoat makers, and trousers makers.

The inauguration of such extreme tax will serve the purpose of diverting trade from the merchant-tailoring industry to the ready-made clothing industry, the majority of whose prices are below the taxable figures. Furthermore, the imposition of such a tax seems unequitable and unwise, for the reason that it is discriminatory—taxing the classes and omitting the masses. If, from the viewpoint that high-grade merchant tailoring is a luxury and should be taxed, as proposed in the revenue bill now before Congress, isn't it probable to assume that many purchasers will discontinue this luxury during the period of the war?

The estimated proportion of people who buy high-grade merchant-tailored clothes has been placed at 10 per cent. When one stops to consider that there are at present some four to five millions of men under arms for the United States, and millions more to be inducted into service by reason of the draft law, the loss in sales to the merchant tailor because of these new conditions is considerable.

It is questionable whether this proposed law will serve the purpose for which it is to be made, for this reason: Assuming that the population of the United States is 100,000,000; that half this number are males; that half of the latter are grown-ups; and when it is estimated that only 10 per cent of the people buy high-grade clothes, the percentage of buyers at this ratio would number 2,500,000. The net income tax on an average sale of \$75 to each of this number at 20 per cent over \$50 would amount to only \$2,500,000.

We are in favor of a 10 per cent tax on all suits and overcoats without regard to prices. Such a tax seems reasonable. It would set aside class distinction, and levy upon all an equal share of the war's liability, and a greater sum would revert to the Government, as the following will illustrate: Assuming that one-half the number of males in the United States are grown-ups, which we will place at 25,000,000, and should each grown-up make a purchase that would average \$40, the net amount that would accrue to the Government on a 10 per cent tax would total \$100,000,000.

Respectfully submitted.

NATIONAL ASSOCIATION OF MERCHANT TAILORS OF AMERICA.
CHARLES F. WETZEL, *President*.

Senator THOMAS. Do you not think that if the manufacturing of clothes for the Army should be increased several millions, it would give all the employment that could be expected for those that may be thrown out of employment?

Mr. WETZEL. There are certain tailors manufacturing clothing from the material furnished by the Government, which is right. It saves profiteering in our materials—

Senator THOMAS. We are going to need all of the tailors we can get.

Mr. WETZEL. I am afraid it will bring the business to the "ready-made."

Senator JONES. What injury would come if it did?

Mr. WETZEL. What injury?

Senator JONES. Yes.

Mr. WETZEL. Well, the fact that I do not think garments will be as well made. They will not have the morale of a well-fitting suit of clothes on an officer. A good-fitting uniform certainly shows authority. Gen. Pershing has mentioned that fact; and we do know that it impresses one. It is commanding. It has authority. If a man is well dressed it shows the morale of the staff as well as the soldiers'.

Senator JONES. I mean in civil life. Why should we not all be wearing ready-made clothes?

Mr. WETZEL. It is a matter of the point of view.

Senator NUGENT. Do you not think that a man who can afford to buy a \$50 suit of clothes would continue to buy clothes of that value, even if this bill becomes a law?

Mr. WETZEL. No. I will tell you why. Our patrons are well supplied with clothes. They like something new. You put into this tax 20 per cent over a certain amount, and they say they will make their old clothes do, and they will virtually do it.

Senator NUGENT. Why is not that a good thing?

Mr. WETZEL. You would practically confiscate a great amount of the tailoring business. Good clothes are not a luxury. It is the experience of all the high-grade tailors that men have said, "You are

a highway robber to charge \$85 or \$90 for a suit." A man said to me, "I thought you were a highway robber to charge \$85 or \$90 for a suit, but when I get out the old vintage of five or six years ago and Jack pats me on the back and says, 'Hello! A new suit of clothes?' I begin to think it is economy." He said, "I was considered a spendthrift for paying \$10 for a pair of shoes, but I have shown the man who called me a spendthrift that mine outwear his three times and four times. They are good leather, well made; they hold their shape."

It is economy to buy quality and good workmanship.

Senator McCUMBER. You wish uniformity in the tax on all clothes?

Mr. WETZEL. We are in favor of taxation; yes, sir.

Senator McCUMBER. You mean to say that a clerk down in one of these departments that is receiving \$4 a day has to wear a certain grade of clothing; his position demands it?

Mr. WETZEL. That is the idea.

Senator McCUMBER. Whereas a workman who is getting \$10 a day and only has to wear overalls, ought to be able to pay a portion of what the \$4 a day man pays for a better suit?

Mr. WETZEL. He is willing to pay. My workmen have all been showing great loyalty, contributing to liberty loans and to the Red Cross fund and all other funds, and I believe all the workmen throughout the Nation, particularly with their increased wages, will all be willing to pay their little tax, whether it is a \$15 suit or a \$20 suit, and we will all be happy to think that everybody will be taxed equitably.

Senator McCUMBER. Not only would be willing to do it, but, considering their means of paying, they ought to do it.

Mr. WETZEL. I think so.

The CHAIRMAN. You have, since the war began, greatly increased your prices, have you not?

Mr. WETZEL. I am glad you spoke of that, because we have received \$90, and we are getting \$100 for a suit of clothes. The statistics show that the materials, linings, workmanship, etc., have been increased from 175 to 195 per cent, and it is not the high-grade tailor that has been able to increase the percentage of what he had to pay, but it is the cheaper grade of tailors. They have taken advantage of it, and they have raised the price 40 and 50 per cent to our 10 or 15. I believe that if you were to set the limit to a \$50 suit of clothes, the man who handles various grade, a \$40 grade and a \$60 grade, is liable to bring down the \$60 grade to the \$50 and the \$40 grade to \$50 in order to make up his deficiency as an average. Who suffers? The public in general, the Government at large, and there is no benefit to anybody.

The CHAIRMAN. The tailors as a rule have all increased their prices—

Mr. WETZEL. Indeed they have.

The CHAIRMAN. But, taking them all together, the percentage of increase has been something like 33½ to 40 per cent?

Mr. WETZEL. In the cheaper grades; yes.

The CHAIRMAN. You say \$40. Has that so discouraged the business that there is danger of some of them having to retire and go into other business?

Mr. WETZEL. No; it has not.

The CHAIRMAN. Has not the business of the tailor been as attractive with those higher prices as it was when the prices were lower?

Mr. WETZEL. It has not.

The CHAIRMAN. It has not been as attractive?

Mr. WETZEL. No, sir. The only thing that has discouraged the tailor at large is his inability to get material or buy to protect themselves—

The CHAIRMAN. You made the point here that slightly increasing the tax on a suit of clothes by imposing this tax will depress the business, and the question I am asking you is whether the increase of 33½ or 40 per cent has depressed the business?

Mr. WETZEL. It has not.

Senator THOMAS. That increase has applied to custom-made goods as well?

Mr. WETZEL. Yes, sir; but the 33½ per cent increase is not the increase of the high-grade tailors.

Senator THOMAS. Your objection is not to the tax, but to the fact that it is imposed only on suits costing \$50 or above?

Mr. WETZEL. Exactly; it is discriminating against a \$50 proposition and 20 per cent above that, and there will be no results. You folks want to get funds by taxation, and the only way to get them is to tax everyone. The men who patronize the high-grade tailors can not get any Norfolk coats or sport coats with belts, etc.

The CHAIRMAN. One of the purposes of the law in imposing this tax is to discourage unnecessary expenditures on the part of the people so as to release that money for other and more essential purposes. You say that this tax will tend to bring about that very result. It would tend to bring about a use by the people in this country of the cheaper grades of goods instead of the higher grades of goods?

Mr. WETZEL. You are not encouraging the people—

The CHAIRMAN. If the effect is to induce people to wear a cheaper class of goods, if that is one of the effects of it, will we not be accomplishing one of the purposes that we have in mind in imposing this tax?

Mr. WETZEL. You are not encouraging economy and thrift. I do not like the word "luxury" in regard to high-grade clothes, any more than a high-grade boot, any more than high-grade furniture against cheap furniture. It is economy and thrift to buy the best quality.

Senator McCUMBER. Your position is that a \$75 suit will last three times as long as one that costs \$40 and there is economy in buying the \$75 suit?

Mr. WETZEL. I know there is. Those are facts.

Senator THOMAS. You do not think a \$50 suit is a luxury?

Mr. WETZEL. I positively do not; and I do not think a \$75 suit or an \$80 suit is a luxury. They contain the best linings and the best material. It is a matter of the point of view, how a man was brought up, so that he probably does not know the difference until he has acquired the habit. I have heard women say, "I wish my boy had never gone to you, because he does not want to wear any other clothes."

I am not saying that because I want to be egotistical, but it is because we are proud to see the old vintages coming in and making

good. They will say, "I will make my old clothes do, because the Government recommends that we can't make Norfolk coats."

The CHAIRMAN. Then, if we impose a tax that will deter men from buying more new suits and tend to make them bring out the old suits that have been thrown away and have them renovated, will we not be subserving a good purpose indirectly from the point of economy?

Mr. WETZEL. Men in general are not buying the same amount of clothes, Mr. Chairman, as they have been heretofore. Where men have bought three or four suits of clothes they will buy one, because they feel that they want to be patriotic, and they will economize. We have to make it up by uniforms that we are making for the officers. That rather fills in the gap.

As I say, I believe that it would be very much better for the Government at large and the consumers and the merchant tailors to have an equitable tax on all clothing.

The CHAIRMAN. Have you anything further to present?

Mr. WETZEL. Nothing else.

Thank you very much.

Mr. LEVI COOKE. Mr. Chairman, Mr. Mayer, of Chicago, would like to discuss the matter of the tax on distilled spirits.

The CHAIRMAN. Very well.

DISTILLED SPIRITS.

STATEMENT OF MR. LEVI MAYER, CHICAGO, ILL.

Mr. MAYER. Gentlemen of the committee, I appear here on behalf of the Distillers' Securities Corporation, sometimes called the Whisky Trust. My client has never appeared here before the House or the Senate in support of or opposing any legislation of any kind at any time. This is the first time that the company through me wishes to submit to you gentlemen some views which may be helpful.

When the question last year of fixing the tax was under discussion, the tax on distilled spirits, some of you gentlemen may recall that, unsolicited, my client addressed a communication to the members of the Senate and the House supporting an increase in the tax. It has never been represented in any hearings, and now for the first time wishes to tell this committee its views so as to prevent, if possible, a disappointment which will be serious.

We have had no hearing before the Ways and Means Committee. We did not appear before that committee, because at that time the question of limitation on the sale of distilled spirits within a particular time had not been enacted by either house. It did not make any difference to us whether the tax was \$1 a gallon or \$8 a gallon, if the Senate and the House concluded that the Government wished to levy a tax of that magnitude. But when we were confronted with the limitation recently passed by the Senate, that on all distilled spirits, inhibiting the sale of distilled spirits after July 1, 1919, we regarded it as our duty to call your attention to some obstacles and difficulties which to us appeared insuperable.

I might add that really there is no selfish purpose in our appearing before this committee, and I think that before I have concluded the remarks which I wish to submit you will probably agree with me.

The so-called Kitchin bill, supplemented by a report filed in the House on September 3, estimates the tax collectible in round numbers as \$800,000,000, \$760,000,000 collected from distilled spirits for beverage purposes, and \$35,000,000 from distilled spirits for other than beverage purposes, which means, I presume, medicinal purposes.

I want to submit some figures to you as to whose accuracy you can get confirmation from the department of Internal Revenue. As near as our estimates, more or less exact, can arrive at a result, there are to-day—and in this the Commissioner of Internal Revenue supports the statement—between 40,000,000 and 50,000,000 gallons of distilled spirits upon which the taxes have already been paid and which are so-called floor goods; that is to say, which are in the houses, on the floors of the wholesalers, distributors and retailers.

There are in bond to-day 138,000,000 gallons, as near as we can accurately arrive at a conclusion. So that in round numbers, there are between 180,000,000 and 190,000,000 gallons of distilled spirits which under the legislation as now proposed, must be disposed of at least to the extent of 100,000,000 gallons in order to realize 800 million tax, and must be disposed of, gentlemen, between now and July 1.

I have no purpose at all in discussing prohibition or antiprohibition on the merits or demerits of either proposition. The client for whom I am talking is engaged to-day in a necessary war industry. He is producing 200,000,000 proof gallons of alcohol or spirits for the United States Government and the allies, all of which is used exclusively in the manufacture of smokeless powder and other munition purposes.

So that, selfishly speaking, the plants of the Distillers' Securities Corporation are to-day engaged not only in a war industry, but are engaged with measurable profit to that company. It owns to-day but a negligible part of the whisky or distilled spirits.

Senator SMOOT. In bond?

Mr. MAYER. In bond or out of bond. I shall be accurate with you, because upon that we can give you the exact statistics. It owns a little over 2 per cent of the total estimated distilled spirits, floor goods, and in bond—quite negligible.

It is making no profit on that. It has a profit, which is substantial. It was a large income-tax payer last year and will be again this year. It purchased five millions of Liberty bonds, and by resolution just passed it proposes to purchase of the new issue two million three hundred thousand. So it will have in its treasury seven millions of Liberty bonds.

We do not come to you as a pauper. We do not come to you to ask for charity at all. We come to give you some views so that in finally enacting the tax legislation you will be guided by such light as we—I can say it advisedly—disinterestedly submit for your consideration. If there were no limitation as to the time within which the spirits, alcohol, whisky, must be sold, we would not be here at all. Eight dollars is a terrific tax. That means \$2 a quart; and if you add the \$2 a quart tax to the cost of bottling, the cost of the material, the expense of handling, you will get your whisky pretty close to \$5 a quart. That is the profit that is made by the distiller, that profit

that is made by the middleman, the wholesaler or jobber, and the profit of the retailer. The manufacturer's profit is very small indeed.

Of the whisky that is in bond, gentlemen, 25,000,000 gallons were manufactured by the Distillers' Securities Corporation, or one of its subsidiaries. But that has been sold. All of the whisky, practically, that it manufactured was sold at a manufacturer's profit.

As you gentlemen know, whisky is not palatable until it is about 8 or 4 years old. Congress itself legislated that whisky in bond can not be bottled until it is 4 years old because it is not palatable. But the manufacturer of whisky, like the Distillers' Securities Corporation, passes it on to the wholesaler or the jobber who buys the whisky the same year, the same season that it is manufactured. He gets his warehouse receipts and pays the cost to the distiller plus a reasonable profit, and this wholesaler or jobber carries the spirits or whisky in the shape of a warehouse receipt, upon which he borrows money from his local bank or bankers.

The Distillers' Securities Corporation does not consume all my professional time. As Senator Smoot knows, I am counsel for the Continental Commercial National Bank, of Chicago, the largest national bank of America outside of New York City. I am counsel for the Federal Reserve Bank of Chicago, and other financial institutions. I have professional knowledge that the buyers of this whisky have not the money to pay for it. They borrow from their local bank or bankers. So that this 138,000,000 gallons of whisky now in bond is probably owned by hundreds, yea, thousands of owners, or the warehouse receipts representing this whisky to a very considerable extent are no doubt held by banks all over the country who have made loans to their borrowers.

Now, if this whisky after July 1 is in bond, it is utterly valueless, because your legislation decrees that after July 1 it can not be sold; it can not be withdrawn from bond. Therefore all of the whisky, the 180,000,000 to 190,000,000 gallons, must be sold between now and July 1—practically all, if the Government anticipates the realization of the \$800,000,000 tax. That is to say, \$8 a gallon is levied upon the whisky which has not yet been taxed and the tax paid. The floor stock, as the proposed act provides, has already been taxed; \$3.20 has been paid on that whisky, and the proposed law provides for an additional tax of \$4.80 when it is used for beverage purposes. So that this body must realize \$600,000,000 by way of tax to conform to the anticipated receipts as shown in the report made by the Kitchin committee to the House.

How are you going to get it? The whisky that is sold is not sold by the distillers to the consumers or to the wholesale grocers or retail grocers or saloon keepers. That whisky is sold to the large jobbers and wholesalers. They have it on their floor. The retailers have it on their floor to the extent of \$40,000,000 to \$50,000,000.

Senator SMOOT. So we will get two hundred millions out of that?

Mr. MAYER. Upon that \$3.20 has already been paid, leaving \$4.80 to be paid on the forty to fifty millions of the floor stock, provided it is all sold between now and the 1st of July. But bear in mind that your law which you contemplate enacting can not become a law in the course of human events until perhaps about November 1. Per-

haps I have accelerated the time in fixing that date between now and November 1. Gentlemen, those who have the money are buying this floor stock from these retailers and wholesalers upon which the tax is only \$3.20, and as near as we can calculate between now and the 1st of November those who own the floor stock will have disposed of a large part of it—let us say all of it, because they are not going to withdraw whisky from bond and pay \$8 tax when they have got on their floor whisky upon which they have already paid \$3.20 and which only requires \$4.80.

Senator SMOOT. To whom will they sell that stock?

Mr. MAYER. To the wholesalers or the consumers, men who want to buy a case of whisky or a barrel of whisky. I am speaking now of between now and the 1st of July. Of course, by the 1st of July they will have been compelled to have sold it all, because what they have not sold is worthless, is valueless, because it can no longer be sold. All this whisky, gentlemen, has been manufactured, this 180,000,000 to 190,000,000 gallons. Let us talk about it as man to man. It has been manufactured with your knowledge, your authority, your consent, and your permission, and the whisky that has been withdrawn from bond has not only been manufactured but purchased with your knowledge and authority and consent. The tax is paid thereon—\$3.20 a gallon.

Let us see the situation in which that is going to place the Government, speaking now from the standpoint of the Government. The whisky on the floor, the so-called floor-stock whisky, will have been disposed of to a large extent. The whisky that is in bond upon which the tax will be \$8 can not, under this law, be withdrawn and the tax paid after October 1. So much of it as is withdrawn and the tax paid must be withdrawn and the tax paid by about June 1, because, gentlemen, with the limited railroad transportation facilities the time of handling property will be ordered withdrawn after June 1, because it will take at least four weeks to have it withdrawn, tax paid, shipped and delivered, as the man who buys it must have it in his store in time to resell it before the 1st of July. Otherwise, what he has on hand is of no value.

Now, gentlemen, this represents a very large sum of money to the banks, to the owners, and those who have bought it for purposes of resale. I can not tell you how much, because I do not know. Some may have paid 90 cents a gallon, some \$1.40 a gallon, and some \$2 a gallon; but hundreds of millions are represented in this commodity which has been produced not only with your full acquiescence but under your knowledge and authority and practically with your direction, because you have taken the tax on it.

I am not here suggesting any change in any of the proposed legislation other than to give you some views which this committee can reflect on and consider before the legislation is final.

Let me make a suggestion, gentlemen. I have told you that my client manufactured 25,000,000 gallons of the whisky that is in bond. That is accurate. That whisky is all owned by purchasers except a negligible per cent to which I have referred. We were compelled under the law to give what is known as a distiller's bond for every gallon of whisky that we manufactured; and by "we" I am speaking merely of this client whose president, Mr. Kessler, is here. We were compelled to give a bond obligating ourselves to pay whatever tax,

gentlemen, you enact; so that if you make it \$8, we are obligated to pay \$200,000,000 on that whisky; and when you have a law which is not modified, changed or repealed, which provides that we must withdraw the whisky after that eight-year period has expired, we are compelled to withdraw it. We have given you a bond that we will withdraw it. That law provides, as does the present proposed law, that the distiller must pay the tax. So that we are obligated under our bonds which are signed by us as principal and by various surety companies as surety, to pay \$200,000,000 in tax, and we are compelled to withdraw it at the expiration of eight years from its entry in that bond, and in this law you say we shall not withdraw it after July 1—

The CHAIRMAN. That bond runs to the Government?

Mr. MAYER. That bond runs to the Government.

The CHAIRMAN. And the Government says that after the 1st of July next you shall not withdraw it. Do you not take it that that will cancel that bond?

Mr. MAYER. There is no repeal in this proposed law, no express repeal, and there can be no repeal by implication, because the very letter of the bond provides that we will pay the tax, and neither an act of God nor of the public enemy is a defense to the payment of that tax at the end of 10 years unless by positive legislation you say we shall not pay it—

The CHAIRMAN. Do you think that there is any ground for serious apprehension, or any apprehension at all, that the Government will attempt to enforce that tax?

Mr. MAYER. There ought to be none; but whatever legislation is enacted ought to contain a provision that the sureties and the principals on the bond shall be discharged from their liability—

The CHAIRMAN. I am not disputing that with you at all.

Senator PENROSE. Have you prepared an amendment?

Mr. MAYER. I have not.

The CHAIRMAN. Suppose you do that.

Mr. MAYER. I am speaking of this—it is unimportant; I mean it is inconsequential—but I am speaking of it as an indication of—I will not say haste, but I will speak of it as indicating how, when you come to closely consider the situation, these incongruities and inconsistencies arise.

But the material, the fundamental proposition that I put up to this committee is that of the 138,000,000 or 140,000,000 gallons of whisky that are in bond, if you keep the limitation of time as July 1 very little of that whisky will ever be withdrawn.

The CHAIRMAN. If I understood you a little while ago, you think that all of it that is on the floor—

Mr. MAYER. Not all, but a large part of it.

The CHAIRMAN. Practically all will be sold before the time this bill passes?

Mr. MAYER. We estimate about 25,000,000 gallons—between now and the passage of this bill?

The CHAIRMAN. Yes.

Mr. MAYER. Oh, no. We estimate about 15,000,000 gallons.

The CHAIRMAN. Then the balance will be subject to this floor tax?

Mr. MAYER. This \$8 tax.

Senator LODGE. It will only yield \$4?

Mr. MAYER. \$4.20 when it is disposed of. But the whisky that is in bond—

Senator THOMAS. \$4.80, is it not?

Mr. MAYER. \$4.80 plus \$3.20.

But the whisky that is in bond will remain there until the war is over, and until demobilization has become effective; and if the national prohibition amendment now being considered and voted on is enacted by 1920 or 1921, this whisky will become absolutely valueless and worthless. I do not believe that the Finance Committee of the Senate means to bring about such a result.

In order that I may not be misunderstood, we are not here to say, "Make the tax \$2 a gallon or \$8 a gallon or \$6 a gallon." But we are here to point out to you the serious, the great disappointment which will confront the country if you proceed upon the theory of realizing \$80,000,000 by way of tax when it is our belief that you will not realize, including the \$4.80 additional tax on the floor stock, in excess of \$200,000,000.

Of course, you will ask yourselves, What is this paid attorney talking to us for? We are anxious that the Government shall realize the largest tax possible that is compatible with any governmental or industrial view. The only course in which you can get the tax that you gentlemen are calculating on realizing is after the floor stock has been disposed of and figuring that that is all disposed of by the 1st of July, there is no stock out anywhere except in bond; and you will have to either make the period a longer period in which the whisky can be withdrawn, or regulate your tax so that it is not prohibitive.

If I may use myself as a concrete illustration, I bought 5 barrels of whisky. I drink very little of it. I do not suppose I take a drink a month. But I have friends at the bar and in the banking business. Mr. Reynolds occasionally gets a case from me, Senator Smoot, and occasionally a judge or some other friend. But I bought the 5 barrels. It was bottled, and I paid \$3.20 tax on it. The whole price, as I remember, was a little under \$1,000. Those who have the means have all done that. Possibly some members of this committee may have been equally as luxuriously extravagant as I have been.

Senator THOMAS. We did it to guard against the possibility of illness in the family.

Mr. MAYER. Unless you provide a tax which will enable this whisky to be withdrawn between now and July 1, or extend the time so that it can not be withdrawn, you will be disappointed to the extent of somewhere near \$500,000,000 in the realization of your tax. That is not guesswork. There are two classes of people who are going to buy this whisky—those who are reckless in their habits or desires and tastes, and those who have the money. But the poor man, the working man, can not put aside a barrel of whisky, which means an investment of \$500, gentlemen.

Senator THOMAS. I should think he could at the present rate of wages in this country.

Mr. MAYER. I have thought that, too, occasionally, Senator, but to speak from my own professional experience, I just got through

the arbitration for the packers of the labor dispute in Chicago, and we found that at the end of three months, with the terrific increase in wages, we have learned from shopkeepers whose places are around the stock yards that a large part of the big wages that they had accumulated during the hearing was immediately expended in what the gentlemen who preceded me said was not a luxury—in high-priced silk stockings, high-priced shoes, high-priced underwear, high-priced clothes.

Senator THOMAS. In other words, they are all improvident.

Mr. MAYER. You have answered it, Senator. I speak from knowledge gained in that case in which I represented the packers in the arbitration hearings.

Senator THOMAS. I think that is true universally.

Mr. MAYER. We have endeavored to be just as helpful as we can. We are not speaking selfishly, because the alcohol that we make—200,000 proof-gallons a day—is not taxed. It is industrial alcohol. We are running full blast in grain distilleries and molasses distilleries. It is not taxed. It all goes to the Government or the Government's allies. I might say that indirectly, possibly, we are selfish, because if this tax which you are calculating on is not collected you will have to put it somewhere, either as a war tax, a profit tax, or a consumption tax—

The CHAIRMAN. Are you meaning to suggest to us that this committee will attempt to override the legislation of Congress as it is contained in the supplementary agricultural bill in case that becomes a law, and present the question anew to the Congress?

Mr. MAYER. No; Mr. Chairman.

The CHAIRMAN. As to whether we will extend the time or not?

Mr. MAYER. No.

The CHAIRMAN. I have not understood you as suggesting that. I want to understand what you are suggesting to us. Are you suggesting that we reduce this tax rate?

Mr. MAYER. I am suggesting that this committee take up with the other department of the Government, the Commissioner of Internal Revenue, and ascertain what will be withdrawn. You need not take our figures. You can ascertain whether it would not be wiser, instead of making an \$8 tax, to make the tax \$3.20, \$4, or \$5—I do not care. I have no suggestion to make, where it will not be prohibitive. In other words, it is your purpose, Mr. Chairman and gentlemen of the committee, as I understand it—it is your anxious purpose to have this whisky withdrawn.

The CHAIRMAN. We want to get the most revenue we can during the period that we are permitted to sell liquor in this country. Your suggestion is that probably we would get more by a resale rate, and that we take that up with the Department of Internal Revenue and see whether their views conform to that.

Mr. MAYER. Our opinion is, and we have considered it from every angle—it is not influenced at all by the personal question; it means no personal gain to us—

Senator JONES. May I ask you a question?

Mr. MAYER. Certainly.

Senator JONES. How much of this whisky in bond was manufactured last year, or is a year old or less?

MR. MAYER. Of the whisky in bond, the production during the last 12 months was under rather than over the 12 months, perhaps. There has been a curtailment in the production of whisky, Senator, in the last three or four years because of the various different States that have gained prohibition.

Senator JONES. My purpose in asking that question was to bring out the fact, if it is a fact, that this whisky in bond varies in value according to its age; and while a man might well afford to pay \$8 tax on whisky which is 4 or 5 years old and which could be consumed and meet the wants, yet, if you take out the whisky that is only a year old and is not fit for immediate consumption, it would make a relatively higher tax on the new whisky than upon the old.

MR. MAYER. Yes, Senator; and in addition to that, that is the argument to which I was about to come. About one-half of the whisky that is in bond was manufactured within the last two years. It is not palatable until it is 4 years old. What dealer or what consumer is going to withdraw whisky from bond when he knows he can not use it? I am not saying "sell" it, because he can not sell it after July 1. He can not consume it. It is not palatable. It is not bottled until four years; and half of the whisky that is in bond, gentlemen, was put there during the last two years.

Senator JONES. Would it relieve the situation any to vary the tax with the respective age of the whisky?

MR. MAYER. I would like to consult just a moment. I am not a merchant or an expert, and I can not answer that. I would not be able to say. Mr. Kessler is the president of the Distillers' Securities Corporation. He says it would not.

Senator JONES. Why not?

MR. MAYER. I can not answer that. Why, Mr. Kessler?

MR. KESSLER. The trade considers whisky as whisky whether it is 1 or 4 years old. The values are the same. In fact, we find in the trade that 6 or 7-year-old whisky is selling for less money in bond than 2-year-old whisky. Whisky is sold on its original gauge. There is an outage, or a loss. Six and 8-year-old whisky is selling for much less money than the young whiskys.

MR. MAYER. If I may supplement that statement: The outage law, the so-called Carlisle law, fixed the amount for which a rebate is allowed. A man not only was buying merely space in the barrel, but was paying the tax and paying the price of the whisky—

Senator JONES. What I had in mind was this: The prospective consumer of whisky who is paying for his own consumption, if he bought 1-year-old goods had to pay some tax on it. If he bought 4-year-old goods, he would be paying a very much larger tax proportionately. Looking at it simply from the standpoint of the possible individual buyer or prospective consumer—because, as I take it, the only hope that you have of selling this 1 and 2 year old whisky at all between now and the 1st of next July is to sell it to a possible consumer?

MR. MAYER. Yes, sir; or a dealer who can resell it to a consumer, because he can not sell it after the 1st of July.

Senator JONES. That dealer could not hope to resell it. Therefore all of this class of whisky must be sold to a prospective consumer, and if he must pay \$8 a gallon on 1-year-old whisky and it will have

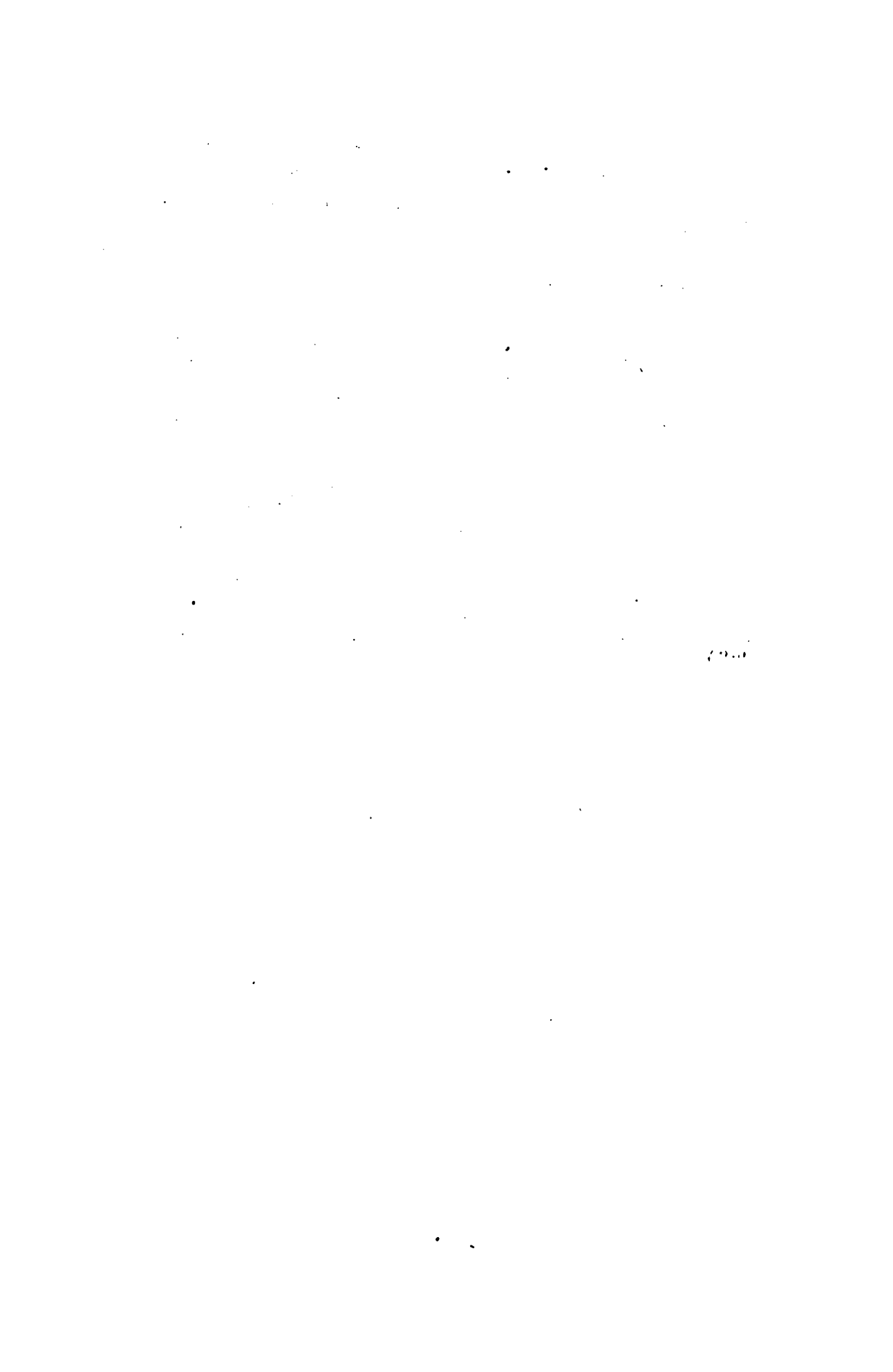
to be held four or five years before he can use it, he is paying more than if he were to buy whisky 2 or 3 or 4 years old.

Mr. MAYER (addressing Mr. Kessler). What is your suggestion as to that?

Mr. KESSLER. The laboring man gets his whisky from the wholesaler through the retailer, and the 2-year-old whiskies are taken by the wholesalers and rectifiers and reduced and made palatable through caramels, sweetened and otherwise; and the 1-year-old whisky is made palatable in that way to be sold more cheaply to the man that can not afford to pay a higher price. Therefore most of the whiskies that are withdrawn as 2 or 3 years old are rectified and reduced and sweetened and made palatable. The real good old whiskies are bought by the richer element of the population of the country.

The CHAIRMAN. I find that there is only one other gentleman who desires to be heard this afternoon. He says he will take only 10 or 15 minutes. I suggested to him that I disliked very much to call Senators back here this afternoon to hear him, and the committee was broken up now, and he has very kindly consented not to press for a hearing this evening, but with the understanding that we will hear him when we first meet in the morning. That being so, we can adjourn until half past 10 o'clock to-morrow morning.

(Whereupon, at 1.25 o'clock p. m., the committee adjourned to meet at 10.30 o'clock a. m., to-morrow, Wednesday, September 11, 1918.)



TO PROVIDE REVENUE FOR WAR PURPOSES.

WEDNESDAY, SEPTEMBER 11, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met pursuant to adjournment at 10.30 o'clock a. m. in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present, Senators Simmons (chairman), Thomas, Jones, Gerry, Nugent, Penrose, Lodge, McCumber, Smoot, Dillingham, and Townsend.

The committee resumed the consideration of the bill (H. R. 12863) "to provide for revenue and for other purposes."

The CHAIRMAN. When we adjourned yesterday morning, Mr. Weil was to have been heard in the afternoon. He was the only gentleman asking to be heard in the afternoon, and by arrangement with him, we did not hold an afternoon session, with the understanding that he should be the first one this morning. If Mr. Weil is present, we will hear him.

ADMISSIONS.

STATEMENT OF MR. MILTON WEIL, 501 FIFTH AVENUE, NEW YORK CITY.

MR. WEIL. Mr. Chairman, I represent the Music Alliance of the United States, of which I am treasurer; the National Music Managers' Association of the United States; and the Musical America Co., publishers of Musical America, a periodical published in the interest of music.

This is an argument on the war revenue tax amending title 7, section 700, of the act of October, 1917, with proposed title 8, section 800, of the proposed war revenue act, on amusement admissions.

I am here representing the Music Alliance of the United States, an organization of which I am the treasurer, which was formed for the purpose of coordinating the various phases of musical activities in this country, which practically represents the interests of 2,000,000 workers in the field.

I will submit in my brief the detailed objects of the alliance.

I also represent as manager, a musical paper known as Musical America, counting among its readers thousands of people throughout the entire country, who are actively interested in music, and regular patrons of the art.

I have been delegated also to represent, in this petition the National Musical Managers' Association of the United States, which

embraces practically every musical manager in the country, representing opera, symphony orchestras, and individual artists.

We wish to submit certain self-evident facts with regard to the musical conditions in this country, so that you will see the exact relation between all this musical activity and its taxable capacity. We also wish to show exactly what effect the proposed 20 per cent tax will have upon the revenue derived from this source.

To avoid any possible confusion in your minds may I define the field represented in this petition. It includes all persons and organizations involved in the giving of orchestral and band concerts, choral and oratorio concerts, song and instrumental recitals and concerts, and operatic performances. This particular petition, I may add, is confined to the interests of those engaged in providing music of the highest class which is of a distinctly cultural and educational character and should not be confused with entertainments of a superficial nature whose sole purpose is essentially for profit and entertainment rather than edification and spiritual uplift.

Measured by gross receipts, from 70 to 80 per cent of all such musical activity of the country: opera, orchestra, recital, choral, etc., is on an idealistic and unselfish basis of "art for art's sake," and it is conducted with invariably a deficit which is made up by devoted individuals—while not more than 20 to 30 per cent of the entire musical activity of the country is speculative in character. Of this nonspeculative volume of business, women's clubs, throughout the United States contribute more than 50 per cent of the total which is on a nonprofit basis. These clubs, which do not make concert giving their regular or continuous vocation, are very timid in their operations, with the result that any apparent change in the usual conduct of their engagements, forces them into discontinuance.

With this situation in your minds, may I point out that while there is no definite basis upon which we can compare the total revenue of admissions to musical performances of various kinds before our entrance into the war, with those under the prevailing 10 per cent tax, there is overwhelming evidence, which I am submitting in my detailed brief, to demonstrate that the present 10 per cent tax has curtailed concert and other musical activities, to the extent of 15 per cent or over. Under the 20 per cent tax, considering the characteristic uncertainty of all such enterprises, it is an inevitable conclusion that further curtailment will result in paralyzing the activities of a large percentage of musical enterprises. Because of discontinuance, this class of public performances will not only yield no increased revenue, but substantially none whatever.

After gathering from every section of the country information through every available source on this subject, we are forced to the conclusion that the revenue under a 20 per cent tax would be considerably less than the present 10 per cent tax has yielded.

While this curtailment of musical activities as it effects the earning capacity of individual musical artists might not seriously affect a few of the more successful and nationally known artists, what would be its effect on that great army of struggling young musical artists, half of whom are women, and many of whom are still in the formative period of their careers, as regards their means of livelihood?

In these few words I have covered merely the dollar-and-cents aspect; behind this there is the great, big ethical question involving music, with so many ramifications that I would not think of taking up the time of your committee to go into it, but which I respectfully submit in the form of this brief.

We urge that music be encouraged rather than restricted in these days of war and stress. That it has the power to solidify public sentiment to stir our patriotism is recognized by our administration.

A short time ago, Mr. John McCormack went to President Wilson, to ask permission to join the great army of American musicians who are singing and playing for our boys in France, and the response to that request was [reading]:

The fountains of sentiment must be kept flowing in this country, and no one can do it as well as you through music.

In conjunction with that, while dining last night I noticed the statement of Gen. Crowder in the evening paper, which I would like to call to your attention, speaking of the registration which takes place to-morrow under the new draft law, as follows (reading):

I want every flag flying and every band playing on registration day.

In this morning paper Mr. Walter Damrosch is quoted as authority for a statement to which I would like to call the attention of the committee, as follows (reading):

BETTER MUSIC FOR PERSHING'S ARMY.

New York, Sept. 10.—Gen. Pershing will soon establish near American headquarters in France a school for bandmasters and musicians in order that the music of American military bands may be of a highest standard, according to Walter Damrosch, director of the New York Symphony and Oratorio Society, who has just returned from France.

Senator TOWNSEND. Your argument applies to music, for instance, such as is given by universities of the country during commencement week and other times, known as music festivals. We have one at Ann Arbor, Mich., and they have called my attention to this, and I ask if you affirm what they have stated to me, namely, that their entertainment is purely educational, and their charge was with an idea of trying to cover expenses, but never did cover expenses.

Mr. WEIL. Never did, Senator, and rarely do any of those. There are thousands of musical clubs in the United States which are supported by women with great big ideas for the uplift of their localities. They engage the artists. The charges for admission in many cases are nominal, because they deal with people of very meager incomes—stenographers, bookkeepers, and people of that class. The tax has curtailed many of those musical clubs, at least 15 per cent or over.

Senator TOWNSEND. Can you tell how much tax was obtained from the 10 per cent provision under the present law?

Mr. WEIL. I can not believe that there is any means of subdividing the tax taken in on amusements. I have tried to figure the thing out, but it is almost impossible. I felt the question would be asked me, and I have endeavored to the best of my ability to try to find that. I believe this, that if the 10 per cent tax is left on music, with the activities that are planned for this coming season, such

activities will materially increase. But if the tax is raised to the 20 per cent, I think I am in a position to say that fully 50 per cent. of that musical activity will have to be stopped this season. For example, the other day at Lockport, N. Y., where they have one of these musical festivals, under the auspices of several rather patriotic men up there in that neighborhood, they have the course system, by which people in meager circumstances for \$10 can get a ticket that takes in all the concerts. Then they have a 25-cent and a 50-cent admission, by which the people can buy individual tickets, as for a violinist or pianist. It is customary for many thousands of these tickets to be sold to these people. At Lockport the other day, through Mr. George W. Pound, who went up there to speak at this festival, I find that the drawers were full of these \$10 tickets. The people had not taken them up on account of even the 10 per cent tax, people who were factory workers, and farmers—music lovers, but who did not feel they could pay that 10 per cent tax, but picked out individual artists that they could get for 50 cents, and they would wait until the next one they wanted to hear, for instance, Mr. Elman, or whomever they wanted to hear. If the 20 per cent tax was on, you would see even less of buying of those tickets. And that represents between 70 and 80 per cent of the music of the country, and would probably means its absolute curtailment, if not wiping it out entirely. But I believe that with the 10 per cent tax left on the musical activities will be greater, because the demand for music is becoming greater and greater all the time, as it is the greatest spiritual uplift there is, and I believe the Government will receive more on a 10 per cent tax than they ever will on a 20 per cent tax.

Senator SMOOT. In your brief, do you propose an amendment to those titles that will bring about the result you desire?

Mr. WEIL. Senator, I have also given that a great deal of consideration, and I can not see how the tax bill could be subdivided to take the speculative and nonspeculative out; and besides, the speculative is such a small per cent of the whole that I do not think it would be material in dollars and cents in the tax bill.

The CHAIRMAN. Will you just let me interrupt you a minute? I find it absolutely necessary for me to be absent for about a half hour or so, and I am going to ask Senator Thomas if he will not take the chair during my absence. I suggest that if members of the committee have not any engagement over in the Senate, that we sit until 1 o'clock to-day.

(Senator Thomas thereupon took the chair.)

(Mr. Weil submitted the following brief, which is here printed in full:)

BRIEF SUBMITTED BY MR. MILTON WEIL, REPRESENTING THE MUSICAL ALLIANCE OF THE UNITED STATES, THE NATIONAL MUSICAL MANAGERS ASSOCIATION OF THE UNITED STATES AND THE MUSICAL AMERICA CO., PUBLISHERS OF "MUSICAL AMERICA," IN CONNECTION WITH HIS STATEMENT AT THE HEARING BEFORE THE SENATE FINANCE COMMITTEE.

MR. CHAIRMAN AND GENTLEMEN: I beg leave here to submit to you in the form of a brief matters supplementing my talk before your esteemed committee.

It is conceded to-day in this country, as it is in every one of the warring nations, and even in the neutral countries of the world, that the greatest factor in maintaining and stimulating the morale of the people at home has been

music, and just as strongly has it been the biggest force in sustaining the morale of the Army and Navy. This has been realized to such an extent that General Pershing has requested that all bands should be doubled in size, and to-day our Army when they march into battle are escorted by a band, and when they come back worn out and tired they go to their rest camps met by a band, as it has been found that music is the greatest mental recreation and restorative for the soldier; that the greatest stimulant to-day that the soldier, well and wounded, is receiving in France, is music in all forms, all of which is officially recognized by our Government.

The tremendous influence of music on the morale of the civilian population is no less than has been demonstrated on the strictly military side, as has been evidenced by the action of the National Council of War Defense throughout this country, for the purpose of stimulating patriotic sentiment, by making us a "singing" nation.

There is not a single phase in the production of this great world war work which is not essentially helped in some way by music. It begins with the recruiting of the soldier; it develops in the training of the soldier in the camp; it is essential with every agency for the raising of funds for the conduct of the war, and in addition every war charity invariably falls back upon music.

Can we afford to allow this agency for the maintenance of morale among both our military and civilian population to suffer?

Can we afford to curtail the musical activities of the country which have done so much for the upholding of the morale of the people, and by their curtailment strike at the very source of the supply, namely: The musical artists and their performances that have meant so much in every development in the carrying on of this war?

It is the purpose of this brief to show both the ethical side as it affects the morale of the Nation and also the practical side of the musical situation, as will appeal to you, gentlemen, from the standpoint of war revenue. Our belief in this contention is based upon thorough investigation made through every available source of information on this subject throughout the country, and we lay before you the following exhibits on this subject:

Exhibit A. Bulletin issued by the Musical Alliance of the United States.

Exhibit B. No. 1, Mr. Charlton's letter; No. 2, statement of Mr. Edw. Ziegler, business comptroller of Metropolitan Opera House; No. 3, letter from Chicago Apollo Club, Miss Mai N. Rea; No. 4, letter from Pittsburgh, Pa. Orchestra Association, signed by Miss May Beegle; No. 5, letter from Albert Steinert, Providence, R. I.; No. 6, letter from Mr. Tom Ward, Syracuse, N. Y.; No. 7, letter from W. A. Fritschy, Kansas City, Mo.; No. 8, letter from Michigan Music Teachers' Association, Lansing, signed by Kate Marvin Kedzie; No. 9, letter from Max Swarthout, Decatur, Ill.; No. 10, letter from St. Louis Orchestra and others, as published in issue of the 24th, signed by A. J. Gaines; No. 11, letter from Geo. W. Andrews, Oberlin, Ohio; No. 12, letter from W. W. Norton, University of North Dakota (published in issue of the 24th); No. 13, letter from Apollo Club, signed by Geo. L. La Vayea, Minneapolis; No. 14, letter from Mrs. Norton Jamison, chairman of club, Los Angeles, Cal.; No. 15, editorial page 18 of Musical America, issue of the 17th; No. 16, letter from Frank W. Healy, of San Francisco; No. 17, California Federation of Musical Clubs, of Los Angeles; No. 18, Federation of Music Clubs of Texas, letter; No. 19, letter from Mrs. George Richards, of Duluth; No. 20, letter from Ferdinand Duncley, Seattle, Wash.; No. 21, letter from Carl Figue, of Brooklyn, N. Y.; No. 22, letter from the Harmony Club, Fort Worth, Tex.; No. 23, copy of letter signed by William G. Frizell, chairman of the Civic Music League of Dayton, O.; No. 24, copy of telegram by F. C. Coppicus, manager Metropolitan Musical Bureau; No. 25, letter (copy) from the St. Cecilia Club of Grand Rapids, Mich.; No. 26, copy of telegram written by E. R. Lederman, president of the Association of Presidents of State and National Music Teachers' Associations.

Exhibit C. Aims of the Musical Alliance of the United States.

We have not submitted naturally all the replies but merely give you sample letters from musical clubs connected with the best musical activities, from the mass of replies received by the Musical Alliance. These have been selected from the different sections of the country and are unanimous in showing that

the proposed tax will paralyze musical activities. It should be remembered these replies are in many cases from persons who are conducting musical activities on a no-speculative and unprofitable basis, as was shown in the hearing accorded the petitioner before your committee.

EXHIBIT A.

The Ways and Means Committee of the House of Representatives, which is revising the war tax schedule, has agreed on a 20 per cent tax on admission to all amusements, which included opera and concerts. This includes also all musical performances which have hitherto been looked upon as educational. According to the judgment of many concert managers, this tax is prohibitive and will mean, not only the contraction of musical schedules throughout the country, but in many cases, the total elimination of such concerts.

The Musical Alliance of the United States stands squarely behind the Government in its plan to win the war by the quickest possible method.

We do not believe, however, that the 20 per cent tax, recommended by the Treasury and now accepted by the Ways and Means Committee, will serve the purpose for which it was devised. It will so reduce the musical activities of the Nation that the proceeds from the tax will be considerably less than they are under the prevailing schedule.

At a time when the musical forces of the country are being marshalled to arouse patriotic interest, for the sale of Liberty bonds, for the raising of funds for the Red Cross, to stimulate recruiting, for the sale of war saving stamps and principally for the establishing of a morale and relaxation of the minds of the people from the strain of the war, we believe that this tax will be a body blow.

We believe that it has been accepted by the legislators without due consideration of its actual significance.

There is only one way to accomplish a revision of this tax measure and that is by a concerted effort to impress the legislators at Washington that the whole musical interests of the United States are united in protesting against it on the ground that the elimination of music would have a bad effect upon the morale of the Nation as a whole.

This means the preservation of our musical life. It can be viewed in no other light.

EXHIBIT B.

B 1.

NEW YORK, August 7, 1918.

MUSICAL ALLIANCE OF THE UNITED STATES,

501 Fifth Avenue, New York.

GENTLEMEN: I inclose you herewith copies of my letters to Senator Calder and Congressman Carew, in regard to the proposed increase tax on admissions.

Cordially, yours,

LOUDON CHARLTON.

AUGUST 7, 1918.

Hon. JOHN F. CAREW,

House of Representatives,

Washington, D. C.

DEAR SIR: In regard to the proposed admission tax of 20 per cent, which will apply to concerts as well as theatrical performances, moving pictures, etc., I wish to emphasize the fact that at least 70 per cent of all the concert business done in the United States is on an "Art for Art Sake" basis, and not more than 30 per cent of the total is speculative in character or for the purpose of making profit. A great mass of this business is conducted by educational institutions, whose only object is to give their student bodies the advantage of hearing the greatest exponents of the best music. These educational institutions are already hit hard by various war exigencies and the doubling of the admission tax will put this class of business out of commission.

Women's musical clubs throughout the United States conduct at least 50 per cent of the total concert business of the country, all of which is on a nonprofit

basis. These clubs are very timid in their operations and doubling the admission tax will likely put most of them out of business for the duration of the war.

An enormous revenue has been realized from concert goers on the 10 per cent tax, but I am positive that the imposition of any tax higher than 10 per cent will result in killing the goose that lays the golden taxes, and, therefore, I am convinced that an admission tax greater than 10 per cent will unquestionably reduce the national revenue from this class of business instead of increasing it, not only as regards concerts, but as regards the theatrical business also. Because of its cheapness, the tax on moving-picture admissions might stand an increase without jeopardizing revenue. But the present tax on concert and theatrical tickets is all the traffic will bear, and any increase will only defeat the purpose of such increase.

Yours, very truly,

AUGUST 7, 1918.

Hon. W. C. CALDER,

United States Senator, Washington, D. C.

DEAR SIR: In regard to the proposed admission tax of 20 per cent, which will apply to concerts as well as theatrical performances, moving pictures, etc., I wish to emphasize the fact that at least 70 per cent of all the concert business done in the United States is on an "art for art sake" basis, and not more than 30 per cent of the total is speculative in character or for the purpose of making profit. A great mass of this business is conducted by educational institutions, whose only object is to give their student bodies the advantage of hearing the greatest exponents of the best music. These educational institutions are already hit hard by various war exigencies and the doubling of the admission tax will put this class of business out of commission.

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Yours, very truly,

B 2.

[From Musical America, Aug. 17, 1918.]

WILL PRODUCE SMALLER REVENUE THAN A 10 PER CENT TAX, SAYS MR. ZIEGLER, OF METROPOLITAN.

The Metropolitan Opera Co. has been watching the tax situation with keen interest. Edward Ziegler, representing the business interests of the company, told a representative of Musical America on Monday that as yet the company was not prepared to make an official statement with regard to its method of procedure in convincing the congressional committees that the 20 per cent tax would be inadvisable, "You may say for me," declared Mr. Ziegler, "that I honestly believe that the Government will collect less money on a 20 per cent tax than it does to-day on the 10 per cent tax."

B 3.

AUGUST 8, 1918.

THE MUSICAL ALLIANCE OF THE UNITED STATES,

501 Fifth Avenue, New York City.

GENTLEMEN: You will find herein inclosed copies of the letter to Senator Sherman and telegram to Congressman Wilson. We earnestly trust this

movement on your part may have the desired end, for we certainly do not want to discontinue our work, which we will be forced to do if this law goes through.

Very truly, yours,

MAUDE N. REA.

CHICAGO, ILL., August 8, 1918.

Hon W. W. Wilson,
Congressman, Washington, D. C.:

As an educational body we most earnestly protest against the 20 per cent concert tax. We make no money even in favorable seasons, existing only to advance musical standards. Such excessive tax will kill this oldest musical organization of Chicago, add no revenue, and cause serious setback to music generally.

THE APOLLO MUSICAL CLUB.

THE APOLLO MUSICAL CLUB OF CHICAGO,
August 8, 1918.

Senator LAWRENCE Y. SHERMAN,
Washington, D. C.

SIR: You will find inclosed a copy of telegram we have just sent to Congressman W. W. Wilson, and we ask that you give this matter your personal consideration.

As a musical organization we have existed for forty-seven years, and have become one of the important factors of Chicago's musical life, but this tax will be our deathblow. The war will not always last, and it is worse than folly to pass laws that will destroy our home institutions.

Our regular season carried through would pay something toward war revenues. If the law passes we give no concerts, and what is gained?

Very truly, yours,

MAUDE N. REA,
Business Manager.

AUGUST 6, 1918.

The 20 per cent amusement tax will seriously affect the musical situation in this country. We are endeavoring to present music as the best relaxation from the strain of war and believe the nation must have music. This increased tax will make it prohibitive for majority. Please endeavor to have an exception made in tax for music.

PITTSBURGH ORCHESTRA ASSOCIATION,
MAY BEEGLE, Manager.

M. STEINERT & Sons Co.,
August 5, 1918.

THE MUSICAL ALLIANCE OF THE UNITED STATES,
501 Fifth Avenue, New York City.

GENTLEMEN: Enclosed please find copy of a letter which I sent to both Senator Peter F. Gerry and Congressman George F. O'Shaunnessey of Rhode Island in regard to the proposed 20 per cent tax on amusements.

Yours, truly,

ALBERT M. STEINERT.

AUGUST 5, 1918.

Hon. PETER G. GERRY,
Senator from Rhode Island, Washington, D. C.

DEAR SENATOR: As manager, financial agent, and sponsor for the Steinert series of concerts which are to be given in New England cities next season, I firmly believe that a mistake would be made in raising the tax on amusements from 10 to 20 per cent. I realize that every effort must be made by the Government and every citizen in order to raise money so that the United States will successfully win the war at as early a date as possible, and I am willing to make every sacrifice and conform with every regulation and rule which is laid down to me by the Government. With an increased rate of taxation there is no question but what numbers of people would not go to amusements, and a greater revenue will be derived by leaving the tax as it is, as the number who patronize

amusements on the 10 per cent would more than offset what would be lost on the 20 per cent basis; local managers could not afford to employ high-priced artists with this anticipated increased rate of taxation, as they would not be patronized by the public, consequently the artist's income would be materially less and the Government would suffer proportionately on their income tax.

There are a number of arguments which could be presented to illustrate the mistake that will be made by raising the rate of tax 10 per cent higher than what it is at the present time, and I hope that you will give this matter your earnest consideration.

Yours, very truly,

ALBERT M. STEINERT.

COPY OF LETTER SENT TO CONGRESSMAN WALTER W. MAGEE AND SENATOR J. M. WADSWORTH.

I understand that the Ways and Means Committee of the House of Representatives in revising the war tax schedule has agreed upon a 20 per cent tax on admission to all amusements, which include concerts and musical entertainments which have hitherto been considered educational. In my judgment this tax will prove to be prohibitive and in most cases will mean the total elimination of such concerts.

The singers and musicians of the United States (with few exceptions) have stood and will stand firmly behind the Government in its plans to bring the war to as speedy an end as possible, but most of us believe that this 20 per cent tax will so reduce the musical activities of the Nation that the proceeds from the tax will be less than they are under the present schedule. The musicians of the country have been called upon, and have gladly and loyally given their time and talents to arouse patriotic interest, to help the sale of Liberty bonds, to stimulate recruiting, and especially to assist in establishing a morale in the minds of the people, and relaxation from the strain of war, and I believe that to them this tax will be a knock-out blow.

I also believe that it has been accepted by the legislators without due consideration of its actual significance.

You might as well eliminate religion as music, and if this tax goes through it will certainly mean just that thing, and I shudder to think of the effect it would have upon the morale of the Nation as a whole.

Trusting that you will do your utmost to have this tax considerably modified, I remain,

Very truly, yours,

TOM WARD,

Conductor of Central New York Music Festival Association.

KANSAS CITY, Mo., August 8, 1918.

The MUSICAL ALLIANCE,
New York City, N. Y.

GENTLEMEN: Many thanks for your circular letter which I found on my desk upon returning to office this morning. The inclosed copy of a telegram which I have sent to both our Congressman and Senator will answer. I sincerely hope that the alliance will be successful in their undertaking. If I can be of any service to you, just say the word.

Sincerely, yours,

FRITSCHY CONCERT DIRECTION CO.,
By W. A. FRITSCHY.

AUGUST 8, 1918.

HON. WM. BORLAND,
Congressman, Washington, D. C.:

Music is the principal factor in establishing the morale and relaxation of minds of the people. We fear that the 20 per cent tax on concerts will mean the contraction of musical activities and in many instances total elimination of concerts. We are also convinced that the returns from 20 per cent tax will be far less than from the 10 per cent tax, as for the majority of people it will be prohibitive. Although loyal to the Government, we earnestly hope you will see this in the true light and not curtail the musical activities of our country by placing a 20 per cent tax on concerts.

LANSING, MICH., Aug. 6, 1918.

THE MUSICAL ALLIANCE,
501 Fifth Avenue, New York.

Am sending copy of telegram sent to local Congressman and United States Senator. "Increased tax on concerts should be opposed by you. Music public necessity in war time. In behalf of 'Matinee Musical' of Lansing this objection is made."

KATE MARVIN KEDGIE.
Mrs. F. S. KEDGIE.

MILLIKIN CONSERVATORY OF MUSIC,
Decatur, Ill., August 7, 1918.

THE MUSICAL ALLIANCE OF THE UNITED STATES,
501 Fifth Avenue, New York City.

GENTLEMEN: I am in hearty accord with the proposal as expressed in your communication of recent receipt to the end that the musical interests of the United States stand squarely against the enactment into a law of the proposed tax on concert admissions.

Accordingly I have instructed the secretary of the conservatory to wire both the Senator and the Congressman representing our district, requesting their aid in the defeat of this feature of proposed war-tax measure recently agreed upon by the Ways and Means Committee of the National House of Representatives. A copy of the telegram is herein inclosed.

Thanking you for the courtesy of your suggestion. I remain, as ever,
Cordially, yours,

MAX V. L. SWARTHOUT.

Millikin Conservatory at Decatur has been providing a series of high-grade artist recitals each year for the past four years, intended wholly to promote general musical appreciation and to provide wholesome recreation for the music lovers of the city and community. Especially now do we feel that such enterprises as these should be encouraged because of their direct and helpful influence on the morale of the people at home. No funds have been available for these concerts other than those provided by a limited subscription ticket sale and by single admissions. The proposed tax of 20 per cent on such admissions as agreed upon recently by the Ways and Means Committee of the National House will in my opinion mean the giving up of the Millikin series after the next season already contracted for. Will you not therefore use your good influence to eliminate the proposed tax that such worthwhile entertainment may live in Decatur?

MAX L. SWARTHOUT,
Director of Millikin Conservatory of Music, Decatur, Ill.

B. 10.

The musical interests of St. Louis learn with regret that the Ways and Means Committee of the House of Representatives, which is revising the war tax schedule, has agreed upon a 20 per cent tax on admissions to all amusements, including opera and concerts.

All loyal Americans believe that the one big thing of to-day is to win the war. Music is a factor to this end. Music has played an important part in sustaining the morale of the Army and of the people at home, in arousing patriotic interest in every form of recruiting, in aiding in the sale of Liberty bonds and in raising a fund for the Red Cross.

Therefore, would it not be disastrous to assess a 20 per cent tax on music, classing music among the nonessentials. Such action would reduce the musical activities of the Nation and the proceeds from the proposed tax will be considerably less than they are under the prevailing schedule.

May we ask your serious consideration of the matter and action in accord with the best interests of our beloved country.

C. W. HUGHES, Apollo Club.
 FREDERICK FISCHER, Pageant Choral.
 JOHN H. GUNDLACH, Pageant Choral.
 CHAS. G. MULLIGAN, Knights of Columbus Choral Club.
 ARTHUR J. GAINES, Manager St. Louis Symphony Orchestra.
 ELIZABETH CUENY, Concert Manager.

ST. LOUIS, Mo., August 10, 1918.

The St. Louis musicians sent this letter to Secretary Paul V. Bunn, of the Chamber of Commerce:

DEAR MR. BUNN: The musical interests of St. Louis have learned with much regret that the Ways and Means Committee of the House of Representatives has agreed upon a 20 per cent tax on admissions to all amusements, a tax which includes operas and concerts.

The Division of Musicians, Artists, and Allied Arts of the Chamber of Commerce, through their committee, requests the board of directors to use their influence with the proper authorities to have this tax kept on the 10 per cent basis which has hitherto been in effect.

We feel that on a 20 per cent basis the musical activities of the Nation will be so reduced that the proceeds from the tax will be considerably less than they are under the prevailing schedule, many of the most helpful musical organizations will be forced to suspend, a large number of people who have spent years of study at their profession be thrown out of labor, and the entire country lose the stimulating and refreshing tonic of wholesome recreation.

Yours, very truly,

CHAIRMAN DIVISION OF MUSICIANS, ARTISTS, AND ALLIED ARTS.

ST. LOUIS, Mo., August 6, 1918.

B 11.

The Musical Alliance of the United States:

Below is a copy of letter sent to the Senator and Representative from this district.

GEORGE W. ANDREWS.

In view of the reported plan to place a 20 per cent tax upon public amusements, including operas and concerts, and also including concerts given for educational purposes, may I respectfully call your attention to the facts below?

The Oberlin Musical Union is the choral organization of Oberlin College, Conservatory, and community. It has been active in the musical life of Oberlin since 1880. It has no endowment, it has sometimes had a surplus, and this has always been used for matters of public need; at present it has a debt of \$1,200 or more; it has been almost upon the point of giving up its work, and would do so except that it now seems possible to find guarantors to enable us to meet our expenses for the present.

If the proposed tax is imposed it will mean, so far as we can see, the absolute giving up of our educational contribution to Oberlin, so long continued.

We are in the war heart and soul, but it seems right that you should know these facts.

OBERLIN CONSERVATORY OF MUSIC.
 OBERLIN MUSICAL UNION.

OBERLIN, OHIO, August 8, 1918.

B 12.

Twenty per cent tax on educational musical performances is a body blow to the greatest means of maintaining morale and promoting patriotism. Not only prohibits musical activities, thus reducing revenue and defeating purpose of tax, but also eliminates potent factor for winning war. Serious situation demands careful consideration. The North Dakota University Male Chorus,

Women's Chorus, Philharmonic Orchestra, Oratorio and Opera Society, band, Norton Chautauqua Orchestra protest against crippling our war service.

WM. W. NORTON,
Director of Music, University of North Dakota.

B 13.

To the Musical Alliance of the United States:

We wish to acknowledge with sincere thanks the receipt of your communication in connection with the proposed 20 per cent tax on all amusements, which include opera and concerts, as agreed upon by the Ways and Means Committee of the House of Representatives at Washington, D. C.

We inclose herewith a carbon copy of one of the letters we have written to our Senator.

This will show to you the attitude we are taking in the matter and we will endeavor to enlist all the aid we can bring to bear in order to secure legislation that will free musical organizations from an unjust taxation and at the same time without opposition to any measure that should fairly be taxed to render a revenue to the Government to help win the war.

We will be pleased to receive from you at all times any information upon such subjects as the above and will gladly render such assistance as we can to further the best interests of your alliance.

Very respectfully, yours,

THE APOLLO CLUB OF MINNEAPOLIS.
GEO. L. LAVAYEA,
Chairman of Concert Committee.

MINNEAPOLIS, August 15, 1918.

B 14.

No class of Americans are more loyal than the musicians and none give more freely of their money and their services. They respond to every call for help from every department of war activities and these calls are almost continuous, for the heads of departments have learned that it is impossible to "put over" anything in the way of effort without music, which is not only an attraction in itself, but which serves as a dynamo to create enthusiasm. Every part of our country is crying for more music, rather than less, and the proposed tax will cripple the interests of musical activities until it will lessen our usefulness to our Government in the time of its greatest need.

We ask for your thoughtful consideration of these things and for your intervention in favor of exempting musical activities from further taxation, which in many instances would be prohibitive.

Mrs. NORTON JAMISON,
President Los Angeles Music Teachers Association.

LOS ANGELES, August 15, 1918.

B 15.

AN OPEN LETTER TO THE MEMBERS OF THE WAYS AND MEANS COMMITTEE, THE MEMBERS OF THE HOUSE OF REPRESENTATIVES, THE SENATE COMMITTEE ON FINANCES, AND THE UNITED STATES SENATE.

GENTLEMEN: Our war is costing us \$50,000,000 of dollars each day. We know that these funds must be raised largely by taxation, by exacting payments from the very processes of our daily life—that so great a sum of money can not be accumulated in the National Treasury unless you, in the fulfillment of your duties, exert the maximum power with which you have been vested to make every phase of our activities pay a proportionate part to the prosecution of a war which we want to see won securely if it finally requires the last drop of blood in the land.

As one of the many means of raising this tremendous amount of money you are now considering the proposal to place a 20 per cent tax on every ticket to a musical performance, concert or operatic. Your purpose in doing this is to

raise money. It is purely a revenue tax and implies no desire on the part of the Government to discourage attendance at such performances.

In the case of the recent railroad mandate, which greatly increased the rates of transportation, it was understood that the purpose was twofold; to raise money and to discourage travel that is not absolutely necessary.

May we be permitted to analyze the situation, to determine whether or not this 20 per cent tax will serve the purpose which your committee has in mind, namely, to increase the governmental funds with which to prosecute the war?

Have you made an investigation to determine the conditions that affect the concert-giving business in the United States? Do you know that the 20 per cent toll you purpose placing on each concert ticket will cause a very large number of concert courses throughout the United States to be eliminated, and that a still larger number will be so curtailed that the total income from the tax will be much smaller than that collected during the last season on a ten per cent basis?

This conclusion is not reached haphazardly. It is based on an investigation made Musical America. The facts will be found in the statements of musical managers printed elsewhere in this issue.

For Example: Let us say that the average monthly income in New York City alone, on a 10 per cent basis, from all tickets to concerts and operas, is \$100,000. If you decrease the attendance by 50 per cent and double the tax you won't increase the Government's revenue and you will deprive a large section of the public from patronizing a form of diversion that has distinctive cultural and education value and which tends to relax strained nerves and establish a healthy, buoyant spirit among the people. Is it sensible? Is it expedient?

Have you made an investigation to ascertain how the 20 per cent tax will affect the incomes, in fact, the very means of livelihood of thousands upon thousands of musicians whose source of personal revenue lies exclusively in these musical performances which you purpose taxing out of existence? Do you know that it will bring poverty to the lowliest orchestral musician, that it will bring distress to the large arm of struggling young concert artists, that it will necessarily be a hardship to the large number of music teachers, that it will greatly curtail the incomes of the more distinguished artists?

Do you realize, gentlemen, that by paralyzing the prosperity of this vast army of workers you would be taking the heart out of one of the most patriotic body of citizens that this war has developed? That they have given bounteously of their time, talent and money to stimulate the public sale of Government bonds, of War Savings Stamps, to the raising of funds for the Red Cross, for the Y. M. C. A., the Knights of Columbus, to Army and Navy recruiting and every other possible agency that contributes to the successful waging of war?

Has it occurred to you that our military chiefs, profiting by the experience of other nations, have asked for more music in the Army and Navy because they know that the psychological effect of massed singing and the playing of bands makes for better, more efficient fighting forces? And do you realize that you can't encourage that musical output by stifling the very means of existence of the musician?

When you tax a business out of existence it is self-evident that that business will not longer yield the funds which are so necessary to support the Government's program. And the men who have given up their whole lives to the musical business are authority for the statement that the 20 per cent tax is virtually confiscatory.

Have you considered the question of the morale of the people?

Behind our wonderful army of fighters in France, in Italy, and Russia, there must be a nation of citizenry, whose morale is at the highest point. It is the knowledge of the existence of this morale that places heart into the heroic work our boys are doing for us at the front. They go into battle with the consciousness that back in the States are a hundred million earnest, sympathetic souls watching their every advance, applauding every achievement, giving un begrudgingly of everything that will hasten the end and bring closer the time when the devastators of liberty shall be brought to their knees.

This morale of the people is a vital thing. It is developed and maintained largely through public gatherings. We have all of us felt the contagion of spiritual uplift, the stimulus of love for our country and its ideals which spring so spontaneously from these inspiring assemblages of the masses. It has been

through this very means that many of us have been constrained to our maximum effort to help win the war.

And in the assembling of the people the musical auditoriums have been the very centers. Is it wise, gentlemen, to curtail that tendency of our citizenry, to foregather by placing a prohibitive tax on the privilege itself? Is it wise to allow the insidious seed of mental discontent, of popular restlessness, to suffer cultivation?

Let's have more music, better music, music everywhere. We can sing our way through the discomfort of war times quite as well as our brave soldiers can sing their way into victorious battle.

But we urge upon you Members of Congress to reject any plan which would throttle the source of that music. It won't raise more money. It will merely impose upon us an essentially unnecessary burden.

B 16.

I am told that the Ways and Means Committee of the House of Representatives has agreed on a 20 per cent tax on admission to amusements.

Being of the opinion that this increase in the war tax would reduce the gross receipts and the Government's earnings, I beg to call your attention to the good work done at the most recent concerts given under my management in San Francisco.

On May 12 and 19 I had concerts by Anellita Galli-Curci at the Exposition Auditorium. From the receipts of these concerts I paid the Government \$3,700 for amusement war tax, and as Galli-Curci created the greatest enthusiasm, we seized the opportunity to make a Red Cross collection. Thus, at but one concert, and by promising to have Galli-Curci autograph all checks received, we ran the total up to \$18,000. I believe that this is a record for a half hour's work.

Would it be possible for us to get \$21,700 at two concerts for the Government and the Red Cross if the amusement tax was increased to 20 per cent? I am quite sure that it would not, and sincerely trust that you will use your influence to see that "well enough" is let alone.

Sincerely,

FRANK W. HEALY.

B 17.

TO THE MUSICAL ALLIANCE OF THE UNITED STATES:

The following letter was sent to the California Representatives at Washington from the California Federation of Musical Clubs:

"The California Federation of Musical Clubs is standing squarely back of the Government in every way for a speedy winning of the war. We sincerely believe, however, that the 20 per cent tax on concerts will strike a serious blow, particularly to the far West.

"Music can hardly be considered in the category of amusements. It is more of an educational force—hence, should not be subjected to the tax levied upon amusements which can be classed as nonessentials.

"Undoubtedly you are aware that the musicians of the country have been importuned upon innumerable occasions to volunteer their services to stimulate interest in all war activities in which the people at large are prone to show little interest. Permit me to particularly call your attention to the fact that the service these people render is their livelihood, and as you know they have always given freely and unselfishly of their talent.

"This tax will also have a tendency toward cutting down attendance, even at concerts of a patriotic nature, which tend to stimulate the national spirit, which is akin to loyalty. At a time when our Government and all musical organizations are fostering these activities to establish the morale and relaxation of the people, we earnestly petition you to use every effort to discourage the enactment of such tax."

Very truly, yours,

BESSIE BARTLETT FRANKEL,

President California Federation of Musical Clubs.

HOLLYWOOD, CAL., August 2, 1918.

B 18.

CORRICANA, TEX., August 17, 1918.

HON. JOHN C. FREUND,

*President Musical Alliance of the United States.**New York, N. Y.*

MY DEAR MR. FREUND: In reply to your call in the last issue of Musical America a telegram, as per copy inclosed, was sent to Texas Senators in Washington and to our Representative, who is a member of Ways and Means Committee. Likewise, letters followed to other Congressmen from our State.

The Texas Federation of Music Clubs heartily indorses this and all other great movements which you are supporting in the interest of music, and we trust that your future plans may include the opportunity for real cooperation with National and State organizations.

It gives me great pleasure to inclose \$1 for an individual membership in the Musical Alliance of the United States.

Most cordially,

(Miss) LOUISE PACE.

President Texas Federation of Music Clubs.

COPY OF TELEGRAM SENT TO TEXAS SENATORS AND MEMBER OF CONGRESS ON WAYS
WAYS AND MEANS COMMITTEE. -----

The Texas Federation of Music Clubs, representing more than 60 musical organizations and an individual membership of more than 1,000, pleads with you to intercede in behalf of music as endangered by the proposed 20 per cent tax. In this time of stress we need music as never before.

(Signed) LOUISE PACE.

President Texas Federation of Music Clubs.

TEXAS FEDERATION OF MUSIC CLUBS, ORGANIZED OCTOBER, 1915.

Affiliated with—

National Federation of Music Clubs.—President, Mrs. A. J. Ochsner, 2106 Sedgwick Street, Chicago, Ill. Southern district president, Mrs. H. H. Foster, Little Rock, Ark.

General Federation of Women's Clubs.—President, Mrs. Eugene Cowles, Los Angeles, Cal.; chairman, music department, Mrs. William D. Steele, Sedalla, Mo.

Texas Federation of Women's Clubs.—President, Mrs. C. W. Connery 1530 Cooper Street, Fort Worth, Tex.

FOREWORD.

In view of the fact that many of the music clubs of Texas do not clearly understand the relation of the Texas Federation of Music Clubs to the Texas Federation of Women's Clubs, a few words of explanation seem expedient.

The Federation of Music Clubs is a separate, distinct and self-governing organization, yet a department of the Federation of Women's Clubs, thereby representing music throughout the State for that organization.

At the annual State and district meetings of the Federation of Women's Clubs, musical programs are provided by the Texas Federation of Music Clubs, this organization being entitled to representation at these meetings, one delegate for every six clubs, delegates being elected by the executive board of the Music Federation.

Active membership dues in the Texas Federation of Music Clubs includes dues with the following organizations: Texas Federation of Music Clubs, National Federation of Music Clubs, Texas Federation of Women's Clubs, music department general Federation of Women's Clubs.

Membership in the State federation is of mutual benefit to music clubs, and to the organization of which it is a part, for in unity only is there strength. The Federation exists for the purpose of promoting music in Texas, which work must be accomplished through cooperation.

President, Miss Louise Pace, 1003 West Third Avenue, Corsicana; first vice president, Mrs. F. H. Blankenship, 3921 Rawlins Street, Dallas; second vice president, Mrs. J. Lee Penn, Waxahachie; recording secretary, Mrs. T. H. Wear, 610 Houston Street, Fort Worth; corresponding secretary, Miss Dorothy Drane, 702 West Second Avenue, Corsicana; treasurer, Mrs. Beatrice Eikel, Kidd Key College, Sherman; auditor, Mrs. Elbert Gibson, 4938 Crutcher Street, Dallas.

BOARD OF DIRECTORS.

Miss Louise Pace, Corsicana; Mrs. F. H. Blankenship, Dallas; Mrs. J. Lee Penn, Waxahachie; Mrs. T. H. Wear, Fort Worth; Miss Dorothy Drane, Corsicana; Mrs. Beatrice Eikel, Sherman; Mrs. Elbert Gibson, Dallas; Mrs. J. F. Lyons, Fort Worth; Mrs. Gae Russell, Sulphur Springs; Miss Ina Hogg, Houston; Mrs. Gentry Waldo, Houston; Mrs. Eugene McNutt, Waco; Mrs. James Hambrick, Tyler; Mrs. R. T. Skiles, Dallas; Mrs. Henry Roberts, Hillsboro; Mrs. W. C. Bule, Marlin; Miss Phoebe Garver, Taylor; Mrs. D. N. Rice, Corsicana; Mrs. Eli Hertzberg, San Antonio.

DEPARTMENTS.

Club extension: Chairman, Mrs. F. H. Blankenship, Dallas; Mrs. George Howard, Houston; Mrs. H. A. Spellings, Jefferson; Mrs. F. W. Snetzer, San Angelo; Mrs. Otis Truelove, Amarillo.

Artist bureau: Chairman, Mrs. Gentry Waldo, Houston; Mrs. J. A. Jahn, Dallas; Mrs. A. L. Shuman, Fort Worth; Mrs. Eli Hertzberg, San Antonio; Mrs. Eugene Haynie, Austin.

Community music: Chairman, Mrs. Eugene McNutt, Waco; Mrs. W. L. Jones, Paris; Mrs. M. Folsom, Wynne, Dallas; Mrs. Rosser Thomas, Bonham; Mrs. T. H. Cheatham, Waxahachie.

Course of study and program exchange: Chairman, Mrs. James Hambrick, Tyler; Mrs. E. P. McConnell, Dallas; Mrs. O. L. Lillienstern, Mount Pleasant; Mrs. Arthur Saft, Austin; Mrs. A. L. Manchester, Georgetown.

Library extension: Chairman, Mrs. R. T. Skiles, Dallas; Mrs. Edna Saunders, Houston; Miss Jeannette Gunst, Corpus Christi; Mrs. Katherine Peeples, San Marcos; Mrs. E. N. Davidson, Jacksboro.

Public school music: Chairman, Mrs. Henry Roberts, Waxahachie; Mrs. N. P. Turner, Marshall; Miss Elfieda Littlejohn, Galveston; Mrs. A. L. Williams, Sulphur Springs; Mrs. D. E. Sanders, Wichita Falls.

Scholarship: Chairman, Mrs. W. C. Bule, Marlin; Mrs. Joseph Morris, Groesbeck; Mrs. T. S. Lovette, Belton; Mrs. J. H. Griffiths, Taylor; Miss Blanche Foley, Houston.

Contest: Chairman, Miss Phoebe Garver, Taylor; Mr. F. Liebke, Brownwood; Mrs. Wade Walker, Wichita Falls; Mrs. J. Allen Kyle, Houston; Miss Aetna Smith, Cameron.

Publicity: Chairman, Mrs. D. N. Rice, Corsicana; Mrs. Willie Hutcheson, Houston; Mrs. Clara Madison, San Antonio; Mrs. Earle Behrends, Dallas; Miss Velma Tisdale, Georgetown.

Program: Chairman, Mrs. Huberta Nunn, Houston; Miss Beulah Duncan, Waco; Mrs. A. D. Bush, Longview; Miss Constance Weldon, Sherman; Miss Edith R. Salyer, Navasota.

SPECIAL COMMITTEES.

State symphony orchestra: Chairman, Mrs. Eli Hertzberg, San Antonio; Mrs. E. B. Parker, Houston; Mr. Carl Venth, Fort Worth; Mrs. Alex Coke, Dallas; Mr. David Holguin, El Paso; Mr. J. S. Cullinan, Houston; Mr. Louis Lipsitz, Dallas.

State festival chorus: Chairman, Mrs. R. L. Cox, Houston; Mrs. Rosser Thomas, Bonham; Mrs. W. L. Jones, Paris; Miss Elizabeth Crawford, Dallas; Mrs. Harvey D. Morris, Port Arthur; Mr. J. Emory Shaw, Paris; Mr. Julius A. Jahn, Dallas; Mr. Hu T. Huffmaster, Houston.

PROGRAM COMMITTEE.

District meetings.—Texas Federation of Women's Clubs: Miss Northern Barton, Denton; Miss Mamie Stowers, West; Mrs. Leon Gross, Fort Worth; Mrs. M. K. Jackson, Colorado; Mrs. Jesse T. Cope, Karnes City; Mrs. A. L. Wilfong, Winsboro.

Army music—Texas cantonments: Chairman, Mrs. Eugene McNutt, Waco; Mrs. M. Falsom Wynne, Dallas; Mrs. T. H. Cheatham, Waxahachie; Mrs. John H. Grant, Houston; Miss Alice E. Holman, San Antonio; Miss Helen Lassiter, Fort Worth.

State eleemosynary institutions.—Chairman, Mrs. Carolyn Carpenter, Fort Worth; Mrs. Wilbur Gibbs, Huntsville; Mrs. Charles Sanders, Austin; Mrs. W. A. Ransom, Corsicana; Mrs. Roy Wilkerson, Hillsboro.

CLUB DIRECTORY.

Alpine.—Alpine Music Club: President, Mrs. T. E. Gillett; corresponding secretary, Mrs. John Gentry.

Anarillo.—Philharmonic Club: President, Mrs. Frank M. Riburn; corresponding secretary, Mrs. W. H. Flamm.

Austin.—Matinee Music Club: President, Mrs. Eugene Haynie, 2511 Whitis Avenue; Corresponding secretary, Mrs. Eugene Schoch, 2212 Nueces Street.

Belton.—Baylor College Choral Club: President, Mr. T. S. Lovette; corresponding secretary, Miss Bessie Booh.

Belton Music Club: President, Miss J. S. Goeppinger; corresponding secretary, Miss Julia B. James.

Bonham.—Chaminade Club: President, Mrs. Rosser Thomas; corresponding secretary, Miss Mary Kenedy.

Brownwood.—Brownwood Music Club: President, Mr. Frederick Libke, Howard Payne College; Corresponding secretary, Mrs. E. M. Andrews.

Cameron.—Symphony Club: President, Miss Aetna Smith; corresponding secretary, Miss Beth Jeter.

Corsicana.—Nevin Club: President, Miss Dorothy Drane; corresponding secretary, Miss Evelyn McKie.

Corpus Christi.—Harmony Club: President, Miss Jeanette Gunst; corresponding secretary, Miss M. Jort.

Crockett.—Cadman Club: President, Miss Evelyn Wall; corresponding secretary, Mrs. S. L. Murchison.

Dallas.—Schubert Club: President, Mrs. R. T. Skiles, 3117 Live Oak Street; corresponding secretary, Miss Grace Anderson, 217 East Twelfth Street.

Music Study Club: President, Mrs. Alex Coke, 3700 Armstrong Avenue; corresponding secretary, Mrs. Charles S. Purnell, 4710 Live Oak Street.

Wednesday Morning Choral Club: President, Mrs. Julian Wells, 4310 Thomas Avenue.

Mickwitz Club: President, Mrs. Joseph B. Rucker, 3209 Douglas Street; corresponding secretary, Mrs. D. C. Tallichet, 3604 Armstrong Avenue.

Tronitz Club: President, Mrs. Earle P. McConnell, 514 Sunset Avenue; corresponding secretary, Miss Lottie Thomas.

Mozart Club: President, Mrs. Earle B. Behrends, 4043 Victor Street; corresponding secretary, Miss Lillie Swann, 301 Hill Avenue.

Ennis.—Bertha Freeman Lewis Club: President, Miss Elizabeth Van Gordon; corresponding secretary, Miss Ina King.

El Paso.—Music Department, Woman's Club: President, Mrs. R. P. Mosson; corresponding secretary, Mrs. F. G. Billings.

Fort Worth.—Harmony Club: President, Mrs. J. F. Lyons, 1411 Hemphill Street; corresponding secretary, Miss Willie Pemberton, 820 Essex Avenue.

Euterpean Club: President, Mrs. C. W. Connery, 1530 Cooper Street; corresponding secretary, Miss Ethel Edwards.

Galveston.—Galveston Choral Club: President, Mrs. Eugene Rosenthal; corresponding secretary, Mrs. Paul E. Nicholls, 1306 Avenue N, 1-2.

Georgetown.—Club of Clefs: President, Miss Velma Tisdale.

Music Study Club: President, Mrs. A. L. Manchester.

Groesbeck.—Kid-Key Music Club: President, Mrs. T. F. Oliver; corresponding secretary, Mrs. J. P. Morris.

Gorman.—Music Club: President, Mrs. W. L. Hohnesly.

Haskell.—Symphony Club: President, Mrs. Richard Nolen; corresponding secretary, Miss Vera Neathery.

Henderson.—Henderson Music Club: President, Mrs. D. E. DeLamar; corresponding secretary, Miss Lucy Mae Yates.

Hillsboro.—MacDowell Club: President, Mrs. Roy Wilkerson; corresponding secretary, Mrs. J. S. Roe.

Houston.—Woman's Choral Club: President, Mrs. Edna Saunders, 1202 Lamar Avenue.

Girl's Music Study Club: President, Mrs. John H. Grant, 1118 Main Avenue; corresponding secretary, Miss Nina Cullen, 1603 Rusk Avenue.

Treble Clef Club: President, Mrs. J. Allen Kyle, Crawford Street; corresponding secretary, Miss Helen Saft.

Jacksboro.—Harmony Club: President, Mrs. E. M. Davidson; corresponding secretary, Mrs. J. H. Curtis.

Jefferson.—Wednesday Music Club: President, Mrs. H. A. Spellings; corresponding secretary, Mrs. G. T. Maggard.

Karnes City.—Karnes City Music Club: President, Mrs. Jesse T. Cope; corresponding secretary, Mrs. A. M. Bailey.

Lampasas.—Harmony Club: President, Mrs. R. S. Mills; corresponding secretary, Mrs. B. C. Greenwood.

Lockhart.—Lockhart Music Club: President, Mrs. John Lipscomb; corresponding secretary, Miss Beatrice Moher.

Longview.—Longview Music Club: President, Mrs. A. D. Bush; corresponding secretary, Mrs. Paul Bramlette.

Marlin.—Wednesday Matinee Music Club: President, Miss Lalla Branson; corresponding secretary, Miss Bernadine Frank.

McKinney.—Junior Etude Club: President, Miss Ruth McKinney; corresponding secretary, Miss Ruth Finch.

Marshall.—Marshall Music Club: President, Mrs. O. E. Busby; corresponding secretary, Miss Lucile Jones.

Mount Pleasant.—Euterpean Club: President, Mrs. R. J. Davis; corresponding secretary, Mrs. T. M. Flemming.

Mexia.—Harmony Club: President, Mrs. Ben Jackson; corresponding secretary, Mrs. George Peyton.

Navasota.—Music Study Club: President, Miss Ira Blackshear; corresponding secretary, Miss Edna Brigrance.

Ozona.—Music Department Woman's Club: President, Mrs. W. E. Newton.

Paris.—Etude Club: President, Mrs. W. L. Jones; corresponding secretary, Mrs. James Yost.

Port Arthur.—Symphony Club: President, Mrs. Harvey D. Morris; corresponding secretary, Miss Jessie C. Miller.

San Angelo.—Music Department, Woman's Club: President, Mrs. A. A. DeBerry; corresponding secretary, Mrs. Culberson Deal.

San Antonio.—Tuesday Musical Club: President, Mrs. Eli Hertzberg; corresponding secretary, Miss Florence Winters.

San Marcos.—Southwestern Conservatory Choral Club: President, Mrs. Katherine B. Peeples.

Sherman.—Kidd-Key Music Club: President, Miss Mozelle Montgomery; corresponding secretary, Miss George Berry Lindsey.

Stephenville.—John Tarlton College Choral Club: President, Mrs. Day Cage; corresponding secretary, Mrs. F. A. Curtis.

Taylor.—Wednesday Music Club: President, Mrs. John H. Griffiths; corresponding secretary, Mrs. E. J. Douglas.

Tyler.—Coterie Club: President, Mrs. A. P. Baldwin; corresponding secretary, Mrs. Thel Williams.

Waxahachie.—MacDowell Club: President, Miss Julia Solon; corresponding secretary, Mrs. E. A. Dubose.

Waco.—Euterpean Club: President, Miss Beulah Duncan; corresponding secretary, Mrs. H. W. Nevin.

Wichita Falls.—Musicians' Club: President, Mrs. N. M. Clifford, 1414 Eleventh Street; corresponding secretary, Mrs. E. H. Maupin, 2315 Ninth Street.

ASSOCIATE MEMBERS.

Capt. Chas. H. Allyn, Corsicana; Capt. James Garitty, Corsicana; Mr. S. A. Pace, Corsicana; Mrs. J. E. Whiteselle, Corsicana; Mrs. Frank Drane, Corsicana; Mrs. Florence C. Flore, Cleburne; Mr. Albert Linz, Dallas; Mr. Herbert Marcus, Dallas; Mr. Alex Sanger, Dallas; Mr. Edward Titcher, Dallas; Mr. R. P. Wofford, Dallas; Mrs. Rita Zane-Cetti, Fort Worth; Mrs. J. S. Cullinan, Houston; Mrs. W. B. Sharp, Houston; Mr. Ellison Van Hoose, Houston; Mr. J. Lee Gammon, Waxahachie; Mr. W. A. Crow, Waxahachie; Mr. J. Lee Pen, Waxahachie; Mr. Roland Harrison, Waxahachie; Dr. T. H. Cheatham; Dr. C. W. Simpson, Waxahachie; Mrs. George W. Coleman, Waxahachie; Mrs. W. D. Anderson, Waxahachie; Mrs. S. E. Fowler, Waxahachie; Mrs. Homer Chapman, Waxahachie; Mrs. T. A. Ferris, Waxahachie; Mrs. R. W. Getzender, Wax-

hachle; Mrs. J. L. McCartney, Waxahachie; Mrs. H. D. Timmons, Waxahachie; Mrs. W. K. Warren, Waxahachie; Miss Alpha Penn, Waxahachie.

HONORARY MEMBERS.

Mrs. Henry B. Fall, Houston; Mrs. Percy V. Pennybacker, Austin; Mrs. J. C. Terrell, Marshall.

CONSTITUTION.

ARTICLE I.—*Name.*

The name of this organization shall be the "Texas Federation of Music Clubs."

ARTICLE II.—*Object.*

Its object shall be to form an established center for the musical organizations of the State, that they may be brought into communication with one another for mutual help and for the advancement of music in Texas.

ARTICLE III.—*Membership.*

SECTION 1. There shall be three classes of membership, active, associate, and honorary.

SEC. 2. All musical organizations of Texas are eligible to active membership, namely, music study clubs, choral societies, festival, and orchestral associations, etc.

Organizations desiring to join the federation shall make application to the first vice president and send to treasurer dues for the current fiscal year.

SEC. 3. Musicians or those interested in the advancement of music in Texas and not affiliated with local musical organizations shall be received as associate members. They may enjoy all the privileges of the federation except the right of voting. Application for associate membership must be made to the second vice president.

SEC. 4. Honorary membership may be conferred by the unanimous vote of those present at any annual meeting.

SEC. 5. Musical sections of department clubs may become federated, provided they comply with the requirements of the constitution and pay dues as individual clubs.

ARTICLE IV.—*Officers.*

SECTION 1. The officers of this federation shall be a president, two vice presidents, a recording secretary, a corresponding secretary, a treasurer, and an auditor. The officers, together with three other elected members thereof, shall constitute the executive board.

SEC. 2. All officers shall be elected by ballot, biennially, a majority of votes cast being necessary to constitute an election.

SEC. 3. No member shall hold the same office more than two consecutive years.

SEC. 4. Vacancies in office may be filled by the executive board until such time as an election is held.

ARTICLE V.—*Meetings.*

SECTION 1. Regular meetings shall occur annually, place and date of meeting to be decided by the executive board.

SEC. 2. The executive board shall meet semiannually, time and place to be decided by the board. Special meetings may be called by the president or corresponding secretary upon request of five members.

ARTICLE VI.—*Representation.*

SECTION 1. The voting body at annual conventions shall consist of the members of the executive board, the chairmen of standing committees, and the president or her appointee, and one delegate from every federated club.

SEC. 2. The chairman of standing committees shall attend all meetings of the executive board and shall be entitled to vote.

SEC. 3. This organization shall be represented at annual meetings of the State Federation of Womens' Clubs by one delegate for every six clubs.

SEC. 4. Music clubs are entitled to representation at biennials of National Federation of Music Clubs by the president of each club or her appointee and one delegate.

ARTICLE VII.—Quorum.

SECTION 1. A majority of the enrolled delegates at the annual meeting shall constitute a quorum.

SEC. 2. Five members of the executive board shall constitute a quorum for board meetings.

ARTICLE VIII.—Amendments.

SECTION 1. This constitution may be amended at any regular meeting by a two-thirds vote, the proposed amendments having been submitted to the clubs of the federation by the corresponding secretary at least one month prior to the annual meeting.

SEC. 2. Amendments may also be made at any annual meeting, without previous notice, by the unanimous vote of all delegates present.

SEC. 3. By-laws and standing rules may be adopted, amended, or repealed at any regular annual meeting by a two-thirds vote.

BY-LAWS.

ARTICLE I.—Dues.

SECTION 1. The annual dues of clubs shall be a per capita tax of 25 cents for active members.

SEC. 2. Orchestral and festival associations, artists' series, or any other musical organizations governed solely by a board of directors shall pay a flat rate of \$10 per annum for membership in the federation.

SEC. 3. Associate membership dues shall be \$5 biennially.

SEC. 4. The Federation shall pay to the State Federation of Women's Clubs, as a department of that organization, dues at the rate of 50 cents per club, 25 cents of this amount to be paid as the assessment to the General Federation of Women's Clubs, and dues as required shall be paid to the National Federation of Musical Clubs.

ARTICLE II.—Officers.

SECTION 1. The regular term of office of all officers shall commence at the adjournment of the annual meeting at which they are elected.

SEC. 2. The duties of officers shall be such as are implied by the respective titles and as specified in these by-laws.

SEC. 3. The president shall preside at all meetings of the federation and of the executive board and shall be a member ex officio of all committees.

SEC. 4. The first vice president shall perform the duties of the president in her absence, shall serve as chairman of the executive committee and receive all applications for active membership.

SEC. 5. The second vice president shall receive application from those desiring to become associate members.

SEC. 6. The recording secretary shall keep a correct enrollment of all clubs, organizations and associate members, shall keep the minutes of all meetings of the federation and the executive board, and shall be the custodian of club reports and other papers belonging to the federation.

SEC. 7. The corresponding secretary shall conduct the correspondence of the federation.

SEC. 8. The treasurer shall be the custodian of all funds of the federation and shall pay out money only upon vouchers authorized by the executive board and signed by the president and secretary. She shall give bond in some bonding company approved by the executive committee, and at the expense of the federation, for the faithful discharge of her duties. The amount of bond shall be decided by the executive committee. Accounts shall be audited annually and a report made at the annual meeting of the federation and at the semi-annual meeting of the executive board.

SEC. 9. The auditor shall audit all bills and accounts of the treasurer and report in writing thereon at annual meetings.

SEC. 10. The executive board shall have supervision over all plans for extending, unifying, and rendering efficient the work of the federation.

ARTICLE III.—Committees.

SECTION 1. There shall be the following committees, consisting of five members each, to be appointed by the executive board:

Course of study and program exchange, community music, library extension, public-school music, artist bureau, scholarship, program, contest, club extension, publicity, and press.

SEC. 2. The course of study and program exchange shall assist clubs in preparing their year's course of study and supervise the exchange of club calendars.

SEC. 3. Community music committee shall encourage the organization of choral clubs throughout the State, with the object of eventually organizing all choral societies into a State festival association, and shall assist in the promotion of good music in all public places operating under municipal license.

SEC. 4. Library extension committee shall assist in the establishment and enlargement of music departments in public libraries, and shall direct a traveling musical library for circulation among the smaller towns and rural districts.

SEC. 5. Public-school music committee shall encourage and assist communities in enlisting the interest of school boards, that music may become a part of school curriculum.

SEC. 6. The artist bureau shall assist clubs in engagement for recitals, that better prices may be obtained, and shall form an exchange of talent among clubs in near-by vicinities.

A list of Texas artists who are active or associate members of the federation shall be compiled for the mutual advantage of both clubs and artists.

SEC. 7. Scholarship committee shall place the free scholarships given to the federation and shall assist and encourage those to whom they have been awarded.

SEC. 8. Program committee shall arrange all programs for annual meetings and provide musical numbers for district meetings of the State federation of women's clubs.

SEC. 9. Contest committee shall conduct all contests of the federation, original compositions, young professionals, contest for the National Federation of Musical Clubs, etc.

SEC. 10. Clubs and extension committee shall assist in the organization of music clubs and interest such organizations in the State federation.

SEC. 11. Publicity and press committee shall attend to the printing of all stationery, circulars, reports, and annular proceedings.

ARTICLE IV.

The fiscal year shall close April 1.

ARTICLE V

All meetings of the federation and of the executive board shall be conducted according to parliamentary rules, as given in "Parliamentary Usages" by Emma A. Fox.

B 19.

DEAR MR. MILLER: I see by the papers that the Ways and Means Committee of the House of Representatives, which is revising the war-tax schedule, has agreed upon a 20 per cent tax on admission to all operas, concerts, etc., including all musical performances which hitherto have been looked upon as educational.

Now, Mr. Miller, this tax is prohibitive and will mean the total elimination of such concerts. The people will reluctantly pay the 10 per cent—now scheduled—but to add anything more means that the concert manager must retire from business.

We do not believe, however, that the 20 per cent tax, recommended by the Treasury Department and now accepted by the Ways and Means Committee, will serve the purpose for which it was devised. It will so reduce the musical activities of the Nation that the proceeds from the tax will be considerably less than they are under the prevailing schedule.

At a time when the musical forces of the country are being marshaled to arouse patriotic interest, for the sale of Liberty bonds, for the raising of funds for the Red Cross, to stimulate recruiting, for the sale of War-Savings

Stamps, and principally for the *establishing of a morale* and relaxation of the minds of the people from the strain of the war, we believe that this tax will be a body blow.

The great army of stay-at-home soldiers—the wives, mothers, and friends of the boys “over there”—must have the relaxation and inspiration gained from the uplift of good music. When all the world is distressed and sorrowful, music is the great source of comfort. Gen. Pershing says, “Music and entertainment are as essential to the soldiers as food and sleep.”

The Matinee Musicale of Duluth and all the musical activities of the city are united in protesting against this added war tax, for the musical life of our country is at stake.

We look to you, Mr. Miller, as our Congressman, to do all in your power to veto this bill, and thereby preserve the musical life of our Nation.

Mrs. CHARLES S. SARGENT, *President Matinee Musical Club.*

Mrs. GEO. S. RICHARDS, *Promoter All-Star Concert Course.*

FRED. G. BRADBURY, *Promoter Popular Artists' Course.*

Duluth, Minn., Aug. 12, 1918.

B 20.

606-608 CHICKERING HALL,
Seattle, Wash., August 16, 1918.

THE MUSICAL ALLIANCE OF THE UNITED STATES (INC.),
501 Fifth Ave., New York.

DEAR SIRS: Herewith I inclose copy of my letter to our Representative in Congress, copies of which also go to our Senators, in response to your urgent appeal received yesterday concerning the proposed 20 per cent tax on all musical entertainments.

If the Musical Alliance succeeds in averting this impending disaster to the musical life of the Nation, it will have brilliantly justified its existence and the vision of its founder.

Not having yet joined its ranks, though having viewed it with favor from the first, I now inclose my dollar for membership.

Yours, very truly,
FERDINAND DUNKLEY.

B 20.

606-608 CHICKERING HALL,
Seattle, Wash., August 16, 1918.

As a member of the national patriotic song committee, Community Singing and Choral Society director, I respectfully beg to declare my conviction that music is essential to the maintenance of the morale of the people during this war, and should be encouraged by every means possible. The proposed 20 per cent tax would undoubtedly prove prohibitive, and thus defeat its purpose of raising war revenue. Not only that, but the repression of thousands of musical entertainments throughout the country in which patriotic music plays a big part would tend very largely to dampen the patriotic spirit of the people which many of us have been working to arouse and sustain. I feel sure that due consideration has not been given to the fact that an injury to the country's musical forces would prove no inconsiderable aid to the enemy.

Yours, truly,
FERDINAND DUNKLEY.

(Author of, and one of the conductors of community singing in Seattle fostered by the Seattle Chamber of Commerce and Commercial Club; conductor Tacoma St. Cecilia Club, and Chehalis Choral Society.)

B 21.

DEAR SENATOR CALDER: If the 20 per cent war tax on concerts should go into effect, I will have to suspend my educational concerts, and music students will be the sufferers.

I know that you can convince your colleagues that there is a vast difference between a cabaret and a classical concert.

Education is ammunition.

Your fellow Rotarian,

CARL FIQUEL

B 22.

HARMONY CLUB,

Fort Worth, Texas, September 3, 1918.

MUSICAL ALLIANCE OF THE UNITED STATES:

We have handled a concert course in our city successfully for several years, but feel that a 20 per cent tax will prove prohibitive.

HARMONY CLUB,

MRS. A. L. SHUMAN, *Business Manager.*

B 23.

We all want to win the war quickly, and so favor all proper taxes, but the proposed 20 per cent tax on admissions to concerts would probably prohibit concerts rather than increase the revenues.

Almost every wide-awake community has some enthusiastic local patriots who volunteer their services in putting on an annual concert course for the purpose of bringing the world's best music within the easy reach of all, and then at the end of the season these same volunteers usually chip in to pay the deficit. Here in Dayton we have the Civic Music League, which undertakes to foster music in our community and to give the finest concerts at the lowest prices. No officer is paid, and any surplus is used in providing more music for the community. Many cities have similar organizations. The 10 per cent tax is now a burden, but we can stand it; a 20 per cent tax would be prohibitive. Can you not help to avert it?

Further, I would call your attention to the exception in section 700 in the present war-revenue tax of 1917, in regard to tax on admissions. It provides: "No tax shall be levied under this title in respect to any admissions all the proceeds of which inure exclusively to the benefit of religious, educational, or charitable institutions, societies, or organizations, or admissions to agricultural affairs, none of the profits of which are distributed to stockholders or members of the association conducting the same."

Under this exception, as a lawyer, I thought, and believe that Congress must have so thought, that a civic music organization with no profits, such as ours, and similar ones in other cities, would be exempt as an educational organization, but the department at Washington ruled that we were simply an amusement organization, and even required us to pay a tax on the 25-cent tickets to the "Messiah," given by combined church choirs on a Sunday afternoon before Christmas, at our Memorial Hall.

As a former legislator, I know that it is difficult for a member of a legislative body to draft an exception to a revenue bill that has any teeth in it after a zealous head of a department gets through interpreting it, but the thought comes to me that, with your legislative experience, you might draw an effective exception that would really exempt civic music and community lecture and concert courses as fully as agricultural fairs are now excepted and exempted.

In behalf of our Civic Music League and the thousands of music lovers in Dayton, to whom the world's best music at popular prices is both a treat and an education, I ask that your thoughtful attention be given to the new tax law on admissions.

Yours, very truly,

WILLIAM G. FRIZELL,

Chairman Civic Music League Artist Concert Committee.

B 24.

The following telegram was sent on Monday to the Ways and Means Committee by the Metropolitan Musical Bureau:

"Honored Gentlemen: The Metropolitan Musical Bureau salutes you and stands squarely behind the United States in winning the war as quickly as possible. We sincerely believe, however, that with a 20 per cent tax on concerts there will be practically no musical life in the country outside of twenty-five principal cities. We urge you to spare this great morale building influence and the thousands of musicians who have been giving their services to the Red Cross, liberty loan, training camps and war stamps. This clause will particularly impoverish struggling young American musicians. We point with approval to the wise course of our neighbor, Canada, in this matter.

"THE METROPOLITAN MUSICAL BUREAU,

"35 West Forty-second Street."

B 25.

To the Musical Alliance of the United States:

Following is a copy of the telegram sent by Mrs. William S. Rowe to Senator William Alden Smith and Congressman Carl E. Mapes. Telegram is as follows:

"In behalf of the St. Cecelia Society of Grand Rapids and the Michigan Music Teachers' Association, I earnestly protest against the proposed 20 per cent tax on operas and concerts recommended by the Treasury Department.

"We believe this tax to be prohibitive and that the elimination of music at this time would have a deterrent effect upon the morale of the Nation.

"Sincerely, yours,

"HELEN BAKER-ROWE."

B 26.

REPRESENT TWENTY-EIGHT ORGANIZATIONS.

The following copy of a telegram is self-explanatory:

M. D. FOSTER, *Congressman,*
Washington, D. C.:

The Association of Presidents of State and National Music Teachers' Associations, with membership representing 28 State organizations, implores you to exert your influence so that the present tax of 10 per cent on musical performances may remain as it is and not be raised to 20 per cent, as proposed by the Ways and Means Committee. Our reason for asking your assistance in this matter is, that we fear the truly educational musical performances would be almost entirely eliminated and that we believe the revenue for our Government would thus be less than at present. Our association stands squarely behind the Government in all its plans to win the war, and our protest is caused from purely patriotic motives.

E. R. LEDERMAN,
President.

CENTRALIA, ILL., August 15, 1918.

EXHIBIT C.

THE MUSICAL ALLIANCE OF THE UNITED STATES (INC.)

John C. Freund, president; Milton Well, treasurer.

Founded to unite all interested in music and in the musical industries for certain specific aims:

1. To demand full recognition for music and for all workers in the musical field and musical industries as vital factors in the national, civic and home life.
2. To work for the introduction of music with the necessary musical instruments into the public schools with proper credit for efficiency in study.
3. To induce municipalities to provide funds for music for the people.
4. To aid all associations, clubs, societies and individuals whose purpose is the advancement of musical culture.
5. To encourage composers, singers, players, conductors and music teachers resident in the United States.

6. To oppose all attempts to discriminate against American music or American musicians—regardless of merit—on account of nationality.

7. To favor the establishment of a national conservatory of music.

8. To urge that a department of fine arts be established in the National Government and a Secretary of fine arts be a member of the cabinet.

Application for membership by those in sympathy with the aims of the alliance, accompanied by \$1 for annual dues, should be sent to Barnett Braslow, Secretary, 501 Fifth Avenue, New York. Checks, Post Office or Express Orders should be made payable to the Musical Alliance of the United States, (Inc.). Banker's Trust Co., depository.

FIRE BRICK.

The CHAIRMAN. Mr. R. P. M. Davis will now address the committee.

STATEMENT OF MR. R. P. M. DAVIS, OF MOUNT UNION, PA.

MR. DAVIS. I do not believe any of us are real speakers, Mr. Chairman. We are manufacturers.

Senator PENROSE. In what business are you?

MR. DAVIS. I am president of the Mount Union Refractories Co., at Mount Union, Pa.

Senator PENROSE. And you speak for the other two, do you?

MR. DAVIS. I have not been appointed to speak for them, but it seems as if they are pushing me forward.

Senator PENROSE. Who are the other two?

MR. DAVIS. Mr. Thomas Kurtz, President of the Standard Refractories Co. at Claysburg, Pa.; and Mr. E. G. Moburg, treasurer of the McPheely Firebrick Co. at Latrobe, Pa.

Senator PENROSE. Will you state briefly what part of the bill you address yourselves to?

Senator THOMAS. Do you speak now for the three, or does each of you wish to be heard?

MR. DAVIS. I speak for the three of them. We wish to speak in reference to the interpretation of the term "capital investment," as it applies particularly to our industry.

We started to appear before the committee as representing only ourselves, but in talking last week to Senator Penrose he suggested we might take this up with those who are also interested in our own industry, with those who are affected in the same manner that we are. These are manufacturers who come from, I presume, about twelve States of the Union. On account of the fact that we were unable to write to them until last Saturday or Sunday, they have not been heard from yet. But I requested that they write directly to Senator Penrose, and I would like to know if their letters could be recorded with this hearing. Is that permissible?

Senator THOMAS. Certainly.

MR. DAVIS. They will represent about twelve to fifteen States.

Senator THOMAS. You want to address yourself to section 325?

MR. DAVIS. Yes.

Senator PENROSE. These concerns are chiefly brickmaking concerns?

MR. DAVIS. They are manufacturers of brick; yes, fire brick.

Senator PENROSE. Through what States are they chiefly scattered?

MR. DAVIS. They are chiefly in New Jersey, Pennsylvania, Missouri, Illinois, Indiana, Ohio, Kentucky. Then they go out into the far West.

Senator THOMAS. I think that business is almost universal.

MR. DAVIS. The fire brick business is confined, I would say, to about twelve or fifteen States of the Union.

Senator THOMAS. My State produces a great deal of them.

MR. DAVIS. In the fire-brick industry there is an association, what is called the Refractors' Association. It includes almost all of the

manufacturers of fire brick. I might state that at the meeting in the association the various manufacturers, in personal conversation with one another, discovered that the law as it stands on the statute books, interpreting capital investment in the manner in which it is now interpreted, took from the largest of our number, from the most powerful, 20 per cent, approximately, of their profits in taxes, and it took from the smallest of our number and from the weakest, about 56 per cent of our profits in taxes, with hardly an exception. That was about the way the rule stood. Whereas if capital investment had been in the law in such a manner that an exemption was not given to water and real money, but only to real money invested, the Government would have received more money in the form of taxes. It would have received it alike from the small and from the large industries.

I was one of the managing directors in one of the large industries, myself, before I went into business for myself, and therefore I know pretty well that with the largest industries the law permits them to get exemptions on a capital investment which consists to a great extent of water, whereas the conservative manufacturer, who has no water in his plant, is exempted for only the real money.

The result of that is that in the fire-brick business there is a variation as regarding the amount of taxes paid, according to the capital investment, of from \$20 per thousand brick annual output, which some pay, to \$123 per thousand annual output. What I mean by that is this, when we were discussing this together, we wondered how we could get at some way whereby, as far as our industry was concerned—and I can not to save my life see why it could not apply to every industry, but there may be reasons—how we could get some equitable way to determine taxes so that we would be treated the same way, nearly alike. Take, for illustration, a fire-brick industry which is standard, in other words, one that has been recently constructed, one that is representative of all the industries to a considerable degree, and appraise that one brick works, have appraisers appraise it, and then they would say that that plant was worth so many dollars, had a capital investment of so many dollars per thousand annual output for that plant.

Senator TOWNSEND. I do not quite understand what you mean by that.

Mr. DAVIS. One plant, we will say, has an output of 50,000,000 brick, and they would say it has a valuation; they would appraise it and get its valuation.

Senator TOWNSEND. According to the output?

Mr. DAVIS. No. They would get what its actual valuation was, first. They would say that plant is worth, we will say, a million dollars.

Senator PENROSE. A typical modern plant?

Mr. DAVIS. A typical modern plant. They would say it is worth a million dollars. That is what it is worth according to appraisal. Now, what is its output? Its annual output is 50,000,000. Then what is it worth per thousand brick? That is what that plant is worth. That is the standard. Then just swing that over the entire industry, and you have appraised only one plant, but you have a fair distribution for every plant in the entire United States.

Senator SMOOT. The same thing applies to every business in the United States?

Mr. DAVIS. Every business in the United States.

Senator SMOOT. That can not be done so easily with other businesses.

Senator PENROSE. Senator Smoot, of course all the members of the committee recognize the difficulties encountered in the definition of capital. But these gentlemen represent a very peculiar situation. Two or three very large concerns get off with a nominal tax, comparatively speaking, and the bulk of them, independents of moderate size, have a tax three or four times that, and it is not amiss to have in the record a glaring case of inconsistency in our definition of capital.

Senator SMOOT. There are thousands of them.

Senator PENROSE. Yes. These gentlemen understand that.

Mr. DAVIS. Yes; it is because there are thousands that we feel that those thousands in some way should have a voice.

Senator PENROSE. Their competitor is the trust, and the trust gets off with 20 per cent tax, and they pay 60 or 70 per cent tax.

Senator TOWNSEND. Do you have a brick trust?

Mr. DAVIS. We would not place on record the statement that there is a brick trust. But there is one large corporation that is very much larger than any other manufacturer in the business.

Senator THOMAS. Let me see if I understand your contention. These large concerns are favored because of the fact that they have issued a lot of fictitious capital?

Mr. DAVIS. I would not put it in that word. I will be specific. The industry that I formerly was connected with, which was organized in 1900, bought a large number of old plants, for which they paid three and four times their real value. They also bought some new plants, for which they paid two or three times their real value. One plant I know had never made a brick, and they paid them about two and a half times what they had paid into their plant.

Senator TOWNSEND. How did they pay them—by stock?

Mr. DAVIS. By part stock and part cash.

Senator PENROSE. They capitalized the goodwill, as they would call it.

Senator THOMAS. Then the capitalization of the company, after these purchases, was larger than the combined capital of the constituents?

Mr. DAVIS. It was for some time. To-day I presume it represents about 40 per cent; not larger than the combined, but it represents, I presume, of the total business, about 40 per cent.

Senator JONES. What is the investment in the ordinary smaller plant?

Mr. DAVIS. That has a great range, Senator. There are in our association plants that would have a capital investment of probably \$150,000. The firm I speak of has a capital investment of about thirty five million.

Senator JONES. The reason I ask that question is that in the House hearings it was suggested by some that there should be a distinction made as to the exemption between a small investment concern and a large investment concern, deeming that the small investment con-

cern depended largely for its earnings on the skill of the management.

Mr. DAVIS. I do not believe that would apply in our industry. I think I can make this proposition—if I am not taking too much time—just a little bit clearer, by getting right down to concrete cases, and that comes to my own. The Mt. Union Refractories Company is a comparatively new company. We started in 1912, and we have expanded very rapidly. We were allowed by the law last year a capital investment of less than \$600,000, according to the original reading of the law. We changed that—which I will not dwell upon, because it does not apply to this case.

We have a modern plant. We have a large amount of raw material, and in proportion to our output we believe larger than the largest manufacturer in the business. We have everything that he has, according to our output, according to our size; that is, the number of brick we make per thousand. We have everything he has. We were allowed originally a capital investment of \$600,000, and it was changed afterwards, and we were granted a larger sum than that, about a million four hundred thousand. Our taxes represented between forty and fifty per cent of our total profits. The largest industry in the business was allowed a capital investment of \$33,000,000. In other words, against, say, a million four hundred thousand, there was allowed thirty-three million. That is his capital investment. How much larger was it than we were? It was eight times our size. It did not have anything—I say this flat-footedly—it has not anything behind it whereby it has any right to more than eight times as large a capital investment as we have.

Senator SMOOT. They give them over 15 times.

Mr. DAVIS. They give them over 15 times.

Senator JONES. I suppose that comes from the fact that the people who now own the larger concern actually put into it that amount of money.

Mr. DAVIS. They bought these old works.

Senator JONES. Yes, and actually paid for them more than they were worth.

Mr. DAVIS. They paid for them in stock.

Senator McCUMBER. Right on that particular point, it does not seem to me that the case you mention would be taken as the actual capital invested. I mean in any case where property is bought for several times its value and paid for in stock and in cash. If you will take section 326 you will find this [reading]:

As used in this title the term "invested capital" means * * *

(1) Actual cash bona fide paid in for stock or share;

(2) Actual cash value of tangible property, other than cash, bona fide paid in for stock or shares, at the time of such payment.

It would seem to me, under that definition, that if the officers of the Government performed their duty, they would not allow a capitalization upon a basis of property purchased for two or three times its value.

Mr. DAVIS. I do not pretend to state here how that capital investment was secured, how that was gotten about, because I have never made it my business to find out, as far as any of my competitors were concerned.

Senator JONES. You are reading from the proposed law, Senator, are you not?

Senator McCUMBER. Yes; this is what we are discussing.

Senator SMOOT. In paragraph 4 of that same section it reads:

(4) Intangible property bona fide paid in for stock or shares prior to March 3, 1917, in an amount not exceeding (a) the actual cash value of such property at the time paid in; (b) the par value of the stock or shares issued.

Senator JONES. The witness was calling our attention to the operation of the present law, and not the proposed law.

Senator SMOOT. They are virtually the same.

Senator JONES. Are they the same?

Senator SMOOT. There is hardly any difference.

Mr. DAVIS. The point we were trying really to bring up was this, that there are in our business certain industries where the capital investment is as low as \$20 per 1,000 annual capacity, and with others as high as \$123 per 1,000 annual capacity.

Senator SMOOT. How much cash did you pay into your concern?

Mr. DAVIS. In our concern we put straight cash throughout.

Senator SMOOT. How much?

Mr. DAVIS. We put all of our profits right back into our plant. We not only did that, but we did not even show them all on our books, because we were trying to run it very conservatively.

Senator SMOOT. You do not answer the question yet. How much cash did you put into the business?

Mr. DAVIS. In our own business, you mean?

Senator SMOOT. Yes.

Mr. DAVIS. I can not answer that offhand, because I do not know.

Senator SMOOT. That is all right if you do not know.

Senator PENROSE. You say it represents an investment of \$600,000?

Mr. DAVIS. Yes.

Senator PENROSE. Did you put that amount in?

Mr. DAVIS. Oh, yes.

Senator SMOOT. The other \$800,000 was profits?

Mr. DAVIS. It was profits and raw material.

Senator SMOOT. They would not allow you to take raw material. By raw material do not mean your beds of clay?

Mr. DAVIS. Yes.

Senator SMOOT. You paid your money for them, did you not?

Mr. DAVIS. Yes, we paid money for them.

Senator SMOOT. They allowed you, then, the increased value after your purchase?

Mr. DAVIS. Yes.

Senator SMOOT. I do not know how they could even do that under this.

Mr. DAVIS. I do not know whether they can or not. There is nothing we did to hide. We did everything in the open. But the point still remains that we are still about one-third of our capitalization against our competitors.

Senator PENROSE. Under this present definition you pay two-thirds more tax per unit output than your competitor?

Mr. DAVIS. I would say about between two and two and a half times as much.

Senator SMOOT. As 8 is to 15.

MINERALS.

The CHAIRMAN. I understand Mr. Callbreath desires to be heard now, so we can hear him.

**STATEMENT OF MR. J. F. CALLBREATH, SECRETARY OF THE
AMERICAN MINING CONGRESS.**

Mr. CALLBREATH. My home is in Denver, Colo., and I am secretary of the American Mining Congress.

Senator THOMAS. You speak in behalf of the precious-metal mines?

Mr. CALLBREATH. In a general way regarding the whole industry. I have prepared my statement in order to conserve the time, and will present it to you. I want to say, though, that I can not speak for the American Mining Congress because of the fact that we are holding no convention during the war period, but what I have to say reflects, as well as I can gather it, the sentiment of various conferences which have been held.

Mr. Chairman and gentlemen, we are engaged in the most costly war which the world has ever known—so far as this country is concerned, the first great unselfish war in history. The responsibility of providing the expense which is necessary to carry on this war is one of great gravity. The Government must have a sum of money so stupendous that the average mind can scarcely comprehend it.

Your first concern will be to provide the required amount of funds; your second, to levy that tax so that no industry producing necessary war materials shall be unduly burdened. The production of minerals is of fundamental importance to all industry at all times and is particularly essential to war operations. It is not only an essential to all activities at the battle front, but it is essential to the production of the food and supplies which are required to maintain the Army. It therefore becomes particularly important that this tax shall be so levied as not to decrease the production of necessary war and industrial minerals.

Mining is a wasting industry. To the extent that it produces, it reduces the original estate. Its invested assets are continually growing less. It is peculiar in another sense, in that it is a short-lived industry and an industry carrying great hazards. All of the possible supply of minerals for all future time is now in existence. A mine with a life of 10 years, each year sells one-tenth of its original holding. The proceeds of that sale appear to be a profit. That part of such proceeds which represents the value of the ore is not profit but rather a transfer of property from one form to another—i. e., a sale of one-tenth of the estate.

I call attention to these peculiar conditions concerning the mining industry, as a basis for some concrete illustrations which I believe will aid your committee in reaching a conclusion as to how the mining industry can be made to pay its full share of the tax required and at the same time so apply this tax as to stimulate that high production of the minerals which are necessary to the effective prosecution of the war.

Every business to be profitable must be able to earn a reasonable return on the capital invested and during the time of its operation pay back the original expenditure. This rule applies to all lines of

business alike. A business which is continuous in its operation has a longer period in which to amortize its investment. The shorter lived the operations, the larger must be the amortization fund. A zinc mine in the Joplin district has an active life of approximately two and one-half years—i. e., a mill by two and one-half years of continuous operation can prepare for market all of the ore within economic hauling distance. A mill with no ore may be worth for removal elsewhere 10 per cent of its original cost. It follows that to make a zinc mine profitable it must be able to earn approximately 50 per cent annually for two and one-half years, to pay back the original investment and a reasonable profit thereon. Such a company must be permitted to amortize the original investment during the life of its operation. Otherwise, a war-profits tax or an excess-profits tax, as provided by the bill under consideration, not only takes all of the profit but a considerable percentage of the original capital.

Under the war-profits provision of this bill deduction is limited to 10 per cent of invested capital (p. 57, sec. 812—par. (b), subdivision 2); and under the excess-profits method deduction is limited to 8 per cent (p. 58, sec. 816).

We believe that this deduction is entirely inadequate in all short-lived mines. To so levy a tax as to take the original investment under the guise of profits would be to paralyze many mining districts and shut off the supply of minerals needed for war and industrial purposes. The Joplin district has a population of approximately 225,000 people—175,000 of whom depend absolutely and entirely upon the zinc-mining industry. Any condition which will prevent development of new mines will in a short time put an end to the industry. This would result, first, in a very serious injustice to the people who live there; second, it would make that community unable to pay a tax in the future; and, third, it would so disturb the zinc market as to bring great burdens to the Government because of the lack of an important war material. The Joplin-Miami district produces more than 40 per cent of the zinc of the Nation. Before the war competitive conditions had depressed the market price of zinc below the average cost, and the production capacity of the zinc mines had been greatly decreased. During the early days of the war, because of the scarcity thus created, the price of spelter in the domestic markets went to a point above 80 cents per pound. To take from the market 40 per cent of our usual supply would necessarily increase the price to a point which would be very burdensome to the Government needing directly and indirectly large supplies of zinc.

A mine or an oil well is a very different property from any other. Owners of mines and wells must seek, find, and extract their product from beneath the earth, and finding a commercially productive mine or well is so rare that many fail where one succeeds. The process of seeking and finding ore in a mine requires an immense expenditure for development work which is not carried to capital account. In the case of a great majority of the smaller enterprises, each mine is owned by a separate company, and can not add to the purchase price of its properties the expenditures for development work and losses sustained in proving other properties to be valueless, an advantage possessed by the large corporation.

The investment needed to extract and reduce ore varies greatly with its mineral contents. When the ore is mined out the capital is absolutely gone. All these facts are taken into account by investors which, recognizing the hazards of these businesses, require an actual income of from 12 to 15 per cent to establish a market value of par, fully double the ordinary interest rates required. The Internal Revenue Bureau of the Treasury Department has recognized this distinction, and I believe it to have been as liberal as it could possibly be under the law in attempting to make the present law meet the Governmental requirements without exacting from owners of mines and wells a greater tax proportionately than other lines of business. The peculiar nature of mines and wells is not fully recognized in the bill under consideration. It defines their "invested capital" just as that of other corporations, giving them no benefit whatever from the discovery and development of new ore bodies.

So far as mines are concerned, the definition of "invested capital," section 325 of the present bill sets a premium on the discreditable devices of the past 20 years intended to work out and inflate book values as the basis for the issue of watered stock, while legitimate mining companies of many years standing, which have charged off their expenditures against operations on the theory that a mine is a wasting property, will be penalized for having done so.

I desire to call attention to one provision of the present law which has worked much of injustice to small companies and possibly has lost the Government much larger sums, which overcapitalized companies have escaped. Section 326 of the proposed act, subdivision "a," subsection 2, contains the following language: "But in no case to exceed the par value of the original stock or shares specifically issued therefor."

To limit "invested capital" to the par value of the stock taken in exchange for property at the time of its acquisition is peculiarly unjust in the case of the smaller mining companies which, in most cases, are organized to own a single mine after its promoters have spent large sums in prospecting and developing. These owners have in many instances acquired and developed a large number of worthless properties before they have developed a productive mine and have expended large sums to put this mine on a paying basis, not by sitting and watching it grow, but by the expenditure of large amounts of money, labor, and energy. It has by this means increased the value of this property and should in all justice be permitted to utilize this increased value in determining its invested capital. Under this part of the section, a company which issues stock conservatively in an amount less than the real value of the property would be limited to such amount even though the property had an actual value much in excess of the face value of the stock, while a corporation which was grossly overcapitalized at the time of the purchase of its property for stock would get the benefit of the increased value of the property up to the par value of the stock issued. This inequity is cured where stock is issued with no par value (sec. 325, par. B, p. 61), but where the fiction of a corporation is used as a convenient means for dividing the interest of business associates and a share of stock represents a certain interest in the property of the corporation entirely uninfluenced by its face value,

it seems entirely evident that this limiting clause can not but work injustice. A specific instance will illustrate:

A few years ago the executor of a New York estate, in order to divide among the heirs a mining property which could not then be properly liquidated, organized a corporation with a capital stock of \$10,000 to which the mining property was transferred and divided the shares in proper proportions among the heirs. In the year 1916 that corporation paid taxes on a capital valuation of \$2,700,000.

Under a strict construction of the present revenue law and under the proposed law, the invested capital of this company upon which it could make deduction is limited to \$10,000, while its actual invested capital is \$2,700,000. Under the proposed law this company is liable to pay 8 per cent of \$2,690,000, or \$215,200 more than it would have been required to pay had its capital stock been fixed at the fair value of its property.

It is understood that the revenue department, recognizing this injustice, has in some instances permitted this excess value to be treated as "paid in or earned surplus," and by this device has avoided the unjust technical requirement of the law. But what assurance can be given that future Treasury officials will be as fair in the administration of the law as those who now serve in that capacity with so much of satisfaction to the public?

It would seem, in view of the large latitude of authority given to the Treasury Department to fix the value of property where the face value of the capital stock exceeds the value of the property, that it can be relied upon to fix a fair value where the face value of the capital stock is less than the value of the property. In other words, the same power in the Treasury Department which is authorized to fix the value of the property of an overcapitalized corporation may be and should be intrusted with power to fix the value of the property of an undercapitalized corporation.

It seems proper to also suggest that settlements made by the Treasury Department in good faith and where all the facts have been presented by the taxpayer should be considered as final settlements. It seems but fair to business interests after meeting all requirements to know that the matters are finally determined.

The strict application of this provision is likely to work an equal injustice to the Government. Let us assume that a mining company had invested \$500,000 in a property and that 75 per cent of its reserve had been worked out prior to January 1, 1917, so that during the taxable year the company had but 25 per cent of its original investment involved. During the year 1917 this company might have made an unusual profit, but under the provision referred to it would be permitted to deduct 8 per cent of the \$500,000 originally invested, instead of 8 per cent upon the \$125,000 actually invested.

Much inequity has resulted from the custom of the revenue department in valuing ore bodies at the purchase price "at the time of such payment," as required in section 326, line 10, page 61. The result of this is to fix different values upon property in all respects absolutely equal in value. Companies A and B own adjoining sections of land of equal but nominal value, for which they respectively paid \$10 per acre. Each at an expense of \$100,000 develop ore, oil or coal reserves worth \$1,000,000. Company B sells its holdings to company C for \$1,000,000. Company A is entitled to a deduction of 8 per

cent on cost of land (\$6,400) and cost of improvements (\$100,000), total \$106,400. Company C is entitled to a deduction on cost of property of \$1,000,000.

This is an abstract illustration, but inequities of this sort will be found in many, if not all, coal districts. This grows out of the proposal that an ore body is worth just what it costs, without regard to the losses in the development of worthless properties, without regard to the hazardous nature of mine development, and without regard to actual value of the property. We submit that there will be a few gamblers at the table where most men lose and where the winner is immediately divested of the rewards of his lucky chance; in other words, that the development of new mining properties absolutely essential to maintaining our mineral supply will not be made except this inequity is provided for and the successful operator is allowed a reward proportionate to the hazard involved in his enterprise.

I might say that if you desire it I would be glad to furnish you with numerous instances of coal mines located absolutely side by side, the properties absolutely the same in every respect, where one company is able to take out three or four times as much as the other.

Senator PENROSE. Has not this matter of depletion in connection with mining companies been taken up with the Treasury Department and this Adams Commission?

Mr. CALLBREATH. Yes.

Senator PENROSE. Have they ever come to any conclusion yet upon the subject?

Mr. CALLBREATH. Of depletion? They have administered the present law in a way that I believe has been counted fair by most of those who have settled with the Treasury Department.

Senator PENROSE. Would not this general question you are touching on come under that process of adjustment in the department?

Mr. CALLBREATH. Except this, there is no assurance that a settlement made with the department under these provisions which does not conform with the law is a final settlement, and there is no reason why a future secretary of the Treasury, or some ambitious politician who desires to make a name for himself—

Senator PENROSE. There are none such around, are there?

Mr. CALLBREATH. There may be.

Senator PENROSE. Not under the present administration, anyhow.

Mr. CALLBREATH. The fact is that there is no assurance that those settlements are final, and if a settlement is made and a deduction is allowed which the law does not authorize, then the people have no assurance that the settlement is final.

Senator PENROSE. Then the mining interests are fairly well satisfied with the equitable adjustment made up to date on their taxes, are they?

Mr. CALLBREATH. As compared with the inequitable law under which the settlements were made. We believe the Treasury Department has done the very best they could to meet the situation, and has in some instances gone around the strict provisions of the law in order to do justice.

Senator PENROSE. Then your only apprehension is that the settlement is not final, and that some one later on could ask for a readjustment of the tax?

Mr. CALLBREATH. That is true, and another reason is that in many instances one man will adjust himself to the strict letter of the law, while another man will apply to the Treasury Department and get a reduction, which works an injustice between the two parties.

Senator PENROSE. Would there be any way of appealing these cases to the court, and if the court affirms the Treasury's decision, would not that be final?

Mr. CALLBREATH. I presume that would be true. Those cases are so numerous that an appeal to the courts of all those who might be aggrieved would burden the courts unduly.

Senator SMOOT. You have been assessed upon interpretations of the law rather than the law itself?

Mr. CALLBREATH. Yes.

An extreme case will illustrate the absurdity of a strict application of this limitation.

Two men each own an undivided one-half of a certain property. These two ownerships were necessarily of the same value and earning the same income. Each of these men organizes a corporation to take over his holdings, each exchanging his rights in the property for all of the capital stock of the company which he organized. One organized a company with a large amount of capital stock. The other organized a company with a small amount of capital stock. The property earned a profit of 8 per cent upon the actual invested capital. One of these companies was obliged to pay a large excess-profit tax, while the other pays no excess-profits tax at all.

Another suggestion as to the proviso in section 30, page 31, line 22. A tax of 12 per cent is levied against net income in excess of the amount distributed in dividends or paid in discharge of outstanding interest-bearing obligations, while profits not so utilized are subject to a tax of 18 per cent. This places a penalty of 6 per cent upon funds held either for necessary working fund or invested in liberty bonds.

We are expecting to place liberty bonds probably to the amount of \$16,000,000,000 during the coming year. A large part of these subscriptions, much the larger part, must come from the large business interests. Bonds bearing $4\frac{1}{2}$ per cent are to be sold to these corporations and a penalty of $1\frac{1}{2}$ per cent is levied against those who meet their patriotic duty. It would seem that this provision should be so amended as to permit corporations to hold necessary operating expenses and to purchase liberty bonds without the infliction of a special penalty.

It would seem that a distinction must be made in assessing a tax upon the earnings of an exceedingly short-lived enterprise, as compared with enterprises of longer life or permanent in their nature. A bill recently passed by the House of Representatives, H. R. 11259, known as the war minerals bill, had for its purpose the stimulation of production of certain minerals necessary in war work, which heretofore have been imported from foreign countries and of which there is now a shortage because of the withdrawal from foreign service of the vessels heretofore engaged in the importation of these ores. We have been importing above 2,000,000 tons of manganese, chrome, and pyrites from Brazil, New Caledonia, and Spain. These minerals are absolutely essential in the manufacture of steel and

explosives. The fact that the supply of these minerals had heretofore come almost entirely from foreign countries, affords some proof that these industries can not thrive at home under normal conditions unless protected by compensating import duties. No one can predict what the tariff policy of the United States will be after the war. In consequence no one is justified in expending a large sum of money for the development of a mine, or the construction of a treatment plant in order to supply a temporary market. If the demand for these minerals shall be terminated in two years, then it is plain that a plant now erected must amortize the original investment during these two years in addition to earning the ordinary profit. The deductions for depreciation can not be made to meet the situation because at the end of the two years a plant might be at least 80 per cent, in which case a 20 per cent deduction for depreciation for the two years would be fair but the remaining value would be entirely valueless unless market conditions justified continued operation.

I do not feel justified in suggesting that these enterprises shall be exempted from war taxes, but, I do urge that full authority shall be given and that this revenue law shall anticipate that deductions for depreciation of plants engaged in short-lived enterprises shall be sufficient to amortize the cost of construction and development during the working period of the enterprise. Operations developed for the purpose of supplying these rare minerals which are needed for war purposes can be more nearly compared to the Government constructed housing facilities and plants constructed for war purposes only, which at the conclusion of the war will be practically valueless. These plants are constructed by the Government because private enterprise can not possibly be induced to create these facilities for the short time during which they may be operated. The same principle applies to the short-life mining operations and unless provisions are made for apparently excessive depletion deductions, these enterprises can not and will not be developed. The same reasoning should apply to all short-lived enterprises whether operations are to be terminated by the want of a market or by the exhaustion of the ore bodies.

Senator PENROSE. You refer to this bill in the Senate. Does your association advocate that measure?

Mr. CALLBREATH. The association has not spoken on that subject.

Senator PENROSE. From your knowledge of the general sentiment among your mining associates, do you think they are in favor of it?

Mr. CALLBREATH. They are very much in favor of the general proposition involved in that bill; that is, the purpose for which the bill is planned.

Senator PENROSE. It carries \$50,000,000, a small sum nowadays, but it is \$50,000,000.

Mr. CALLBREATH. But not too much, if the Government shall undertake to purchase the supply of these minerals which are required.

Senator PENROSE. Have you examined the bill?

Mr. CALLBREATH. Yes, sir.

Senator PENROSE. Personally do you approve of the bill in its details?

Mr. CALLBREATH. I do not.

Senator PENROSE. I only ask these questions, Mr. Chairman, because we know we are called upon, by grinding taxes, to raise this money from the taxpayers, and I think maybe we can make an incidental reference to some of the expenditures.

Senator THOMAS. I think the question is quite pertinent.

Mr. CALLBREATH. I should be very glad to discuss that bill.

Senator PENROSE. I personally should like to have some illumination on that.

Mr. CALLBREATH. My thought is that all of these minerals which are essential to the country at this time, which can not be produced under ordinary conditions, should be provided by the Government in that way; and that those minerals can be produced. New enterprises can not be created for a period of a few months or a year or two unless some plan is devised by which the cost of the plant can be amortized during the period of the life of that operation. That would be impossible under a two or three year plant, unless the amortization fund be very large. We have been importing from Brazil approximately a million tons annually of manganese ores. We have abundant supplies of manganese ores in this country but of low grade, and it will be necessary to treat that ore in order to bring it up to the high standard required by the steel industry, and the cost of the treatment and the development of the processes for treatment are expensive. It would be bad business for any private concern to undertake to build a plant and work out the processes of treatment and reduction for a market which two years from now could be taken away by cheaply mined ore bodies in Brazil, with a freight rate of \$2 per ton to our shores.

Senator PENROSE. Why, in this one crisis, when labor is very scarce, is it not economically wise to purchase this material from Brazil, which is a nation with which we are at peace?

Mr. CALLBREATH. If we can get it.

Senator PENROSE. You say we are getting it.

Mr. CALLBREATH. We have been getting it, but that supply has been shut off because the ships which have heretofore transported it have been put into foreign service.

Senator PENROSE. Then this bill is in a measure to protect American industry at home?

Mr. CALLBREATH. I would not call it that.

Senator PENROSE. It savors of that. It has that aroma.

Mr. CALLBREATH. It is a bill to develop industries at home which can not stand after the war unless protection is afforded.

Senator PENROSE. Then it is our duty during this war crisis to bolster up some defunct mining propositions so that they can stand on their feet after the war. Is that it?

Mr. CALLBREATH. No, Senator. My thought is that the low-grade manganese ores, running 15 to 18 per cent, of the great ranges in Minnesota, which can be developed to meet our requirements here at home, should be developed, and if I were to express my personal opinion, I would say that after the war is over such a protective tariff should be levied as to enable those activities to continue.

Senator PENROSE. I heartily agree with you. But the present party in power disagrees with you.

Senator LODGE. I know something about the matter of manganese, which is just as you have stated. I should like to ask you if your

association regards fuller's earth, chalk, kaolin, and sulphur as unusual minerals which require Government aid?

Mr. CALLBREATH. It seems to me that there are many elements included in the provisions of that bill which ought to be eliminated.

Senator SMOOT. I shall offer an amendment to eliminate them to-day.

Senator PENROSE. Are there many that ought to be included that are omitted?

Mr. CALLBREATH. I think not, Senator.

Senator PENROSE. I kind of suspected you did think there were some.

Mr. CALLBREATH. No. My belief is it should be confined to the war minerals—

Senator PENROSE. I am glad my mind is relieved.

Mr. CALLBREATH. Which we are not able to import at this time.

Senator NUGENT. Do I understand that in your judgment that statement represents the opinion of the gentlemen engaged in the mining industry of this country?

Mr. CALLBREATH. I think it does represent a large percentage. Of course, there is a difference of opinion as to the wording of the bill, but I think the belief was practically universal that the Government should undertake to supply minerals in the best way that it could to meet the requirements.

Senator TOWNSEND. Do you understand that some of these minerals are produced necessarily as a sort of a by-product, or in connection with other minerals, and that Government control over some of these minerals, for instance, some qualities that are obtained from iron, would also mean the taking over of the iron mines?

Mr. CALLBREATH. I would think not. But I should certainly want the bill to be so worded that it could not be supposed to do that, even.

Senator SMOOT. I have an amendment that I will offer to-day, which I think will be accepted, that will take care of that.

Senator JONES. I would like to state in this connection that the purpose of that bill, among others, was to provide for the increased supply which is necessary during the war of many of these metals, and which will not be necessary after the war. There are a good many of those metals which are used in very much larger quantities during the war than will be necessary after the war is over.

Mr. CALLBREATH. That is true.

Senator JONES. And the purpose of the bill is to provide largely for that situation.

Senator PENROSE. Do you think gold and silver ought to be included in the bill?

Mr. CALLBREATH. I do not.

Senator PENROSE. Do any of your associates?

Mr. CALLBREATH. I think not. I am just about to come to a discussion of the gold situation.

Senator THOMAS. Your time has really expired, but we have been interrogating you, and you can have 10 minutes more, with the consent of the committee.

Mr. CALLBREATH. Gold mining is the one business which is burdened by prosperity in other lines. When financial systems can be so arranged that gold is not the basis of credit, this will become a

matter of small concern to the public. So long, however, as gold is the basis of our currency, it becomes essential that the proper ratio between credit money and gold shall be maintained in order that our credit at home and abroad may be preserved.

At the present time gold production throughout the world is falling off at a rapid pace. With the exception of a very few high-grade gold mines, the production of gold (except in association with other minerals) is rapidly coming to a standstill. The cost of gold mining in the Western States has increased fully 60 per cent during the last three years. The value of the product remains the same. The gold production of the United States during the last three years is as follows: 1915, 101,053,700; 1916, 92,316,100; 1917, 84,456,600; a falling off of approximately 10 per cent annually. The decrease during the present year will greatly exceed the ratio of the last three years.

My own belief is that it will be fully three times as great as the ratio of the last three years.

Senator THOMAS. The ratio will decrease?

Mr. CALLBREATH. Yes; the percentage of decrease.

Senator LODGE. What do you estimate would be the total production of gold in the United States and Alaska?

Mr. CALLBREATH. I think it would be less than sixty millions annually from this time on.

The great low-grade gold-producing mines of the country must close unless some special aid is given them, because they can not continue operation under the present increased cost without any increase in production.

Senator PENROSE. Why would it not be a good idea to aid those low-grade mines in this bill and let them share in the benefactions of the \$50,000,000 fund?

Mr. CALLBREATH. I do not think \$50,000,000 would be sufficient to cover the situation.

Senator PENROSE. We could add two or three hundred millions to it—just raise the taxes a little more.

Senator SMOOT. One of the objections to this bill is that it does not have enough appropriations.

Senator PENROSE. We could extend the war appropriation for six months and maybe get enough money to keep the gold mines open.

Mr. CALLBREATH. This situation as to low-grade gold mines will not be affected by the proposed revenue bill, because these mines have no profits to tax. Gold must command the serious attention of your committee.

A foundation sufficient to sustain a certain structure of credit may be found entirely unable to sustain a vastly increased credit. The United States is more fortunate than any other nation in the world in having a surplus share of the world's gold reserves. It will need to guard that reserve with intelligent foresight.

In the enactment of a revenue law providing for the collection of a tax amounting to 80 per cent of the total gold in the world and two and one-half times our own gold reserve, every possible precaution must be made to keep up the replenishing stream of gold production. There are those who advocate that gold mining shall be ex-

empted from the excess and war profit taxes. I would rather urge you to so assist the gold-mining industry that it shall be able to pay taxes. If your committee can not see its way clear to give serious consideration to some future legislation of this character, then I believe that gold mining should be exempted from the requirements of this bill. High-grade gold bodies are not numerous and are usually developed as the result of very great expense and long and tedious operations. Then, the high-grade gold body is exhausted in a very short time. An ore body which has been sought for 10 years and which may be exhausted in one is a losing proposition if that production shall have been made at a time when the Government takes 80 per cent of the net operating revenue as a tax. If that production had been scattered during the 10 years of development work, there could be no objection to making that business stand its full share of tax in proportion to other lines of industry, but, when the returns of 10 years' effort are charged only with the expenses of 1 year, the injustice is self evident.

I believe your committee may well consider that phrasing of the proposed bill as will enable the owner of such a mine to amortize the original capital and investment during the life of the mine. While this subject is not under consideration at the present time, I am willing to go upon record with the prediction that before many years not only this country but other countries will find it expedient to provide special inducements for the production of gold from low-grade deposits, in order that a stable foundation may be provided for the rapidly expanding credits which are necessary in our industrial life, and which, because of war conditions, are being accelerated with frightening rapidity. A million dollars in gold taken from the ground forms a reasonably stable basis for \$8,000,000 of currency.

I hope your committee will pardon this reference to a condition perhaps outside the domain of your present consideration, but one which, in my judgment, will command your attention in the near future.

In order that the suggestions which I have made may be in practical form, I desire to submit concrete suggested amendments which will cover the points referred to and, as we believe, add to the effectiveness as a revenue measure of a bill possessing many features to commend it.

(The suggested amendments referred to above are here printed in full, as follows:)

I. The 6 per cent differential tax on undistributed profits should be eliminated. (See sec. 230.)

The tax of 6 per cent additional on undistributed earnings penalizes the corporation that invests its surplus in Government bonds or retains it in the business. The provisions of the present law should stand, allowing the investments in business or the reasonable requirements therefor or in Government obligations without extra tax. (See sec. 10 b of present law.)

II. The proposed law fails to allow to new corporations a credit of the normal profits limiting it to 10 per cent on capital invested. This discriminates against all corporations with no prewar record and takes 80 per cent of their profits over 10 per cent. An example will make this clear:

Two corporations with invested capital of \$1,000,000 each, (1) one with prewar earnings of 15 per cent, and a taxable income of 15 per cent, (2) the other without a prewar record but with similar income.

The tax computed as follows (specific exemption omitted for simplicity):

(1) Old company would not be taxed under the war profit method and the tax under the excess profits method would be as follows:

New income	\$150,000
Credit 8 per cent of capital	80,000
Income taxable at rate of 35 per cent	70,000
Tax	24,500

(2) New company will be taxed under war profit method as producing a higher tax:

Net earnings	\$150,000
Credit 10 per cent of capital	100,000
Taxable at 80 per cent	50,000
Tax	40,000

This amendment gives credit for all cash or tangible property paid in for stock or otherwise.

V. New ore bodies.

The life of a mining corporation depends on the continued discovery and development of new ore bodies. This is a corollary from its wasting nature. It exists by consuming its deposits. It must obtain new ore bodies or die.

Therefore mines should be allowed in "invested capital" the value of newly developed fields. These new ore bodies are not an appreciation in value of old capital assets. They represent new capital produced by the skill, energy, and expenditures of the miner and prospector.

We suggest an amendment that remedies the defect.

Amend section 326 (a) by adding to subdivision (3) the following words:

"*Provided*, That in the case of mines, oil and gas wells there shall be included in surplus a reasonable amount to represent the value of after developed ore bodies or deposits; said amount to be determined under rules and regulations to be prescribed by the commissioner with the approval of the Secretary."

VI. The tax when assessed and paid in good faith should be final.

We propose an amendment to section 1201 that secures this:

Amend section 1201 to read as follows:

"That the Secretary or the commissioner may and on the request of any taxpayer directly interested shall submit to the board any question relating to the interpretation or administration of the internal-revenue laws, or involving the assessment or determination of any tax thereunder, and the board shall report its findings and recommendations to the Secretary or the commissioner, as the case may be, and such findings on any question involving the determination or assessment of the tax shall when approved by the commissioner be final unless set aside by a court of competent jurisdiction."

VII. Section 336 of the proposed bill prohibits consolidated returns.

This should be stricken out and some proper provision adopted permitting affiliated returns. Many mining corporations are subsidiary operating companies with identical ownership and intertransactions with a parent company making it all one business. The Treasury Department has recognized the necessity of such by article 77 of regulations 41.

There is no reason for such discrimination. Neither makes a war profit. Whatever figures are adopted this discrimination follows.

We propose the following amendment, which will place new corporations on an equal basis:

Amend section 312, subdivision (b), to read as follows:

"If the corporation were not in existence during the prewar period, or if it had no net income for the prewar period, then the war-profits credit shall be the sum of:

"1. A specific exemption of \$3,000; and

"2. An amount which bears the same ratio to the net income of the corporation for the taxable year as the war-profits credit, under paragraph 2 of subdivision (a) of representative corporations for the taxable year, engaged in like or similar trade or business, and having net income in the prewar years, bears to the net income of such representative corporations; but in no event to be less than 10 per cent of the invested capital of the corporation for the taxable year."

III. The proposed law fails to recognize the extra hazard incident to mining. The mining industry presents two marked characteristics which distinguish it:

- (1) Its wasting nature.
- (2) The extra hazard.

The law makes a satisfactory provision for the first by a depletion allowance (see sec. 234, subdivision 9). It ignores entirely the risk.

The following proposed amendment permits a classification of mines according to the hazard:

Amend section 316 by adding, at line 22, the following words:

"*Provided*, That in the case of mines, oil and gas wells, the excess-profit credit shall consist of a specific exemption of \$3,000, plus an amount not less than ten or more than twenty-five per centum of invested capital, such percentage credit to be determined by the Commissioner of Internal Revenue under such rules and regulations as he may prescribe."

IV. The limitation of the invested capital to the par value of the stock should be stricken out.

To effect this we suggest the following amendment:

"Section 326. Amend subdivision (a) by substituting, in lieu of subdivisions (1) and (2), the following:

"(1) Actual cash paid in;

"(2) Actual cash value of tangible property, other than cash paid in at the time of such payment, but if paid in prior to January 1, 1914, the value as of such date."

This amendment also restores the provision in the present law providing properties of older companies as of January 1, 1914.

The invested capital of all of the older corporations has been already arrived at by the Treasury Department. The bill as proposed will require a reappraisal and, in many cases, at a remote date when data is unavailable.

Senator LODGE. Mr. Callbreath, speaking to you as a man familiar with mining and with metals, I should like to ask you about some of these which are classed here as rare and unusual elements.

Chalk is mentioned. I never heard it called a rare and unusual element before. I always supposed it was plentiful.

Mr. CALLBREATH. I would consider it so. But I am not posted as to the reasons why the War Industries Board believes that those elements should be included.

Senator PENROSE. Is chalk a military necessity?

Mr. CALLBREATH. I do not know what the purpose of it is.

Senator LODGE. Then we have phosphorus, which I know exists in this country in great quantities; fuller's earth, which I suppose exists in every State.

I am picking out some of these that strike me as war necessities, being referred to as rare or unusual elements.

Mica. That we are familiar with in connection with the tariff. It exists in North Carolina in large amounts; also, to a certain extent, in New Hampshire. Of the others, of course some of them are obviously rare. Phosphorus, pyrites, sulphur—

Senator SMOOT. Do not forget sulphur.

Senator LODGE. Kaolin, of which I suppose there are mountains in this country.

Do those strike you, as a mining man, as rare and unusual elements?

Mr. CALLBREATH. I feel that there is no reason why those should be included in this bill unless there is some shortage of which I am not aware.

Senator LODGE. Of course we all know that tungsten and uranium and vanadium are rare metals.

Senator JONES. There has been more trouble about sulphur than almost any one of the other metals mentioned in the bill.

Senator SMOOT. It is a question of transportation.

Senator LODGE. The question of sulphur is one of the most troublesome things that we have to deal with.

Senator SMOOT. Transportation and cost.

Senator LODGE. It is not rare and unusual.

Senator SMOOT. Oh, no.

Senator PENROSE. You say that you favor in a general way this pending proposition?

Mr. CALLBREATH. Yes, sir.

Senator PENROSE. Do you refer more particularly to the House bill or the Senate bill?

Mr. CALLBREATH. I was very much in favor of what was known at one time as the Henderson bill, which left out very much that is in the present bill.

Senator LODGE. This is the Henderson bill.

Mr. CALLBREATH. This was another Henderson bill.

Senator PENROSE. With all due respect to Mr. Henderson, this is the Baruch bill.

Mr. CALLBREATH. It was prepared largely by the War Industries Board, and Mr. Henderson's original suggestion was added to very largely, and many ingredients interpolated and a different method of administration of the bill proposed. I was heartily in favor of the first bill, and I feel doubtful as to this, although I do believe, gentlemen, that it is absolutely necessary that this Government shall provide the means by which those elements which are needed now for war purposes shall be provided, and I do not think it is possible for independent enterprises to build a plant and to provide for the production of the ore when, at the end of two years, the market will be at an end.

Senator LODGE. I mentioned sulphur and mica in connection with the tariff. I happen to know that there are great quantities of it. I know that in Louisiana they have stepped aside a little from the true faith, and I am afraid that North Carolina was a little weak on mica.

Senator THOMAS. In other words, the tariff is a local question.

Senator LODGE. Very largely.

Senator PENROSE. Do you know whether there is any alarming scarcity in grinding pebbles?

Mr. CALLBREATH. Yes, sir; that is a very important proposition.

Senator PENROSE. Where are they found?

Senator THOMAS. They are found chiefly in Belgium and Holland.

Senator PENROSE. Are there none in America?

Senator THOMAS. There are, but comparatively few that are sufficiently hard for the purpose. They are getting some of them now on the Pacific coast. They were also using steel balls up to the time it was necessary to cut them off because of the demand for steel elsewhere. But the Belgian and Holland sea pebbles are the only natural rock that had been found hard enough for that purpose.

Mr. CALLBREATH. I thank you, gentlemen, very much for listening to me so patiently.

Senator THOMAS. Now, Mr. Thompson, we can give you 15 minutes. It is our intention to take a recess at 12 o'clock.

**STATEMENT OF MR. A. SCOTT THOMPSON, ATTORNEY AT LAW,
MIAMI, OKLA.**

Mr. THOMPSON. Mr. Chairman and gentlemen of the committee, my name is Thompson. I speak here this morning for the lead and zinc producers of three counties, known as the Joplin-Miami mining district. Ottawa County is in Oklahoma, Cherokee County is in Kansas, and Jasper County is in Missouri. That is known as the Joplin-Miami zinc and lead field. The bulk of the production of zinc in that district to-day is being produced in my home county in Oklahoma. It is comparatively a new field that is producing. Three counties produce 40 per cent of the zinc in the United States to-day.

In behalf of those producers I want to contend that the lead and zinc mining in that field is of such a character that it is entirely different from the ordinary business, because of its hazards, because of the risks incident to that business.

I have here, which I would like to have placed in the record, a statement that has been carefully prepared by representative operators in my district, showing the brief financial history of all completed mines in that district.

There are 175 mining ventures in my district that have been completed and reached the producing stage. I offer this for the purpose of confirming my statement that mining in this district, while it is producing large quantities of zinc, averages to be a very hazardous business.

This statement will show to you the moneys actually put into each venture, giving the name of the venture, the location of the district, giving you the time that the property was operated after it reached the point of production, showing the loss or the profit in each venture and the disposition of the plant.

And in this table I want to call your attention to the fact that the calculations are based upon the profit or loss, merely the production profit or loss. No allowance is made whatever for depletion, depreciation, or amortization.

Mining in our district, like a great many other districts, does not pay or has not heretofore paid much attention to technical accounting, and this is an account of just the result.

In each of the 176 mines that we furnish you the financial history of there was something over five millions of dollars invested. This record shows—certified by a responsible man—that that total investment netted a net profit of \$6,600, or an average profit of \$37 per mine.

Less than 10 per cent of the mining ventures in our district reach the producing stage. Less than 25 per cent of those which do reach the producing stage get their capital returned to them.

I do not want the committee to understand that we have no good mines; that we have no mines that do not yield substantial returns. They do. But I am speaking of the average. I think the extreme life of any individual mine in our field would be six years.

In presenting that, gentlemen, we are objecting to being classed, for the purpose of deduction, with the stable substantial business of banking. With this record I hardly think that there would be very much banking if the financial history existed in that institution as in mining.

Senator TOWNSEND. What you say in reference to lead applies to every mine, more particularly to coal in Missouri. The amount of money invested in the mining ventures is a great deal more than the total output that comes to investors?

Mr. THOMPSON. I think so; yes sir. But there is a distinction in our district even with reference to lead properties. For instance, in reference to the lead properties in southeast Missouri, the deposits are much more uniform and larger in extent. The life is many, many times what the lead deposits are in our field. Our life is extremely short. The average life is two and three-fifths years.

What we urge is this, in our amendments, that we object very seriously to the definition of invested capital being limited to the cash paid in for stock and property exchanged for stock not to exceed the par value of the stock. We urge in the amendments offered by Mr. Callbreath that invested capital, not alone in mines but every property, pay the cash put in and the value of the property in the investment.

I fail to see wherein there is any justification at any time for limiting the value of property to the par value of the stock. We have many small ventures in our district where the capitalization is nominal, not to exceed \$6,000. Yet the property is worth a half-million of dollars, exchanged for the stock.

With this technical limitation and with a deduction of 8 or 10 per cent on the par value of the stock, the deduction amounts to nothing on a property value—

Senator JONES. You say that is the value of the property now. Was it the value of the property when the company was organized?

Mr. THOMPSON. Oh, yes. That is all we contend for, Senator, that we have the value of the property at the time of payment or transfer to the company. That is all we are asking for.

Senator JONES. But what are you going to do with the prospector who has a mere prospect which he is developing, and he suddenly comes upon a very valuable body of ore. Do you not think that the law as it is in its definition of capital works an injustice to that fellow?

Mr. THOMPSON. There is not any question about that, Senator.

Senator JONES. There is that feature which you want us to consider carefully, and I think you are quite right in making the request.

Now, your next point is that the mining industry as a whole is a hazardous business?

Mr. THOMPSON. Yes, sir.

Senator JONES. And that the exemption from an excess profit tax or a profit tax should take the hazardous character of the business into consideration in allowing the exemption?

Mr. THOMPSON. Yes. We offer one amendment to the exemption or the deduction clause of the present bill, providing for, in the case of mines and oil and gas wells, a deduction of from 10 to 25 per cent to be assessed within the discretion of the Treasury Department.

Senator JONES. Do you think it advisable for us to enumerate in this bill the different industries and fix the amount of exemption for each line of industry, or do you think it advisable that some tribunal be created or the Treasury Department delegated with authority to ascertain the usual normal incomes of these various lines of industry which they should ordinarily receive, which would be a reasonable return in normal times of the industry, taking into consideration its hazardous character and allow exemptions upon that basis?

Mr. THOMPSON. To answer that, Senator, I would much prefer that the power be conferred upon the Treasury Department or some board authorized to investigate.

Senator JONES. I also see in your statement that in the lead industry a part of it has become stabilized by the finding of large bodies of ore, working on a regular output basis and having a fixed cost, whereas other lead mines are in largely the development period, and with different classes of deposits and, necessarily, are more hazardous than the other class of lead producers. You think there should be some means established whereby a distinction could be made even as between the lead producers?

Mr. THOMPSON. Oh, yes. For instance, in our field we have a zinc property. The normal return on a successful plant is far in excess of 10 per cent. The life is short. Taking into consideration the hazard of the general business, we in normal times would have 50 or 75 per cent return on the actual capital in that particular investment.

There are zinc mines in other parts of the country where the deposits are more uniform and equal and larger in extent, where possibly 10 per cent normal return would be more nearly correct.

So, then, there must be a classification, and I think it is impossible within the bill to classify the business. I should think that the English system is more nearly correct, that a board of referees be allowed to extend to these classes additional deductions.

Just one point that I wanted to raise with regard to the provision in the war profits provision which allows an old corporation actual prewar earnings and a new corporation 10 per cent on capital invested. In my field 95 per cent, because of the short life of the property, are new operations. They have all come into production since the war. That is a very unfair discrimination against new corporations, because the old corporation in our field must make a great deal more than 10 per cent.

We suggest in one of our amendments that new corporations be allowed the same credit that a representative corporation with a prewar record that was similarly circumstanced secures. Justness requires that they have an equal credit. As a matter of fact, I have figured out in the present bill that all new corporations will fall under the war profits plan.

Just one other feature that is particularly applicable to my State. Our constitution prohibits corporations owning real property outside of cities and incorporated towns. Just why that was done, I do not know; but that is part of the constitution. That makes it impossible for corporations to own real property, own the fee, own possibly a mining lease excepting such as they are actually conducting operations upon. The result is that as the companies grow they are forced to form holding companies to hold their holdings, and

then they develop a piece of property, usually not to exceed 40 acres, to determine its minerals, and they organize a subsidiary company owned by the same men. I know some very good mines out there, and I know one organization that has these operating mines separately incorporated, the operating end of it. None of them are organized for more than \$6,000 capital stock, par value—corporations that have paid as high as 6,200 per cent dividends in the last two or three years.

This bill prohibits the filing of a consolidated return, although that is the original business owned by the same men in the same proportions. This bill at page 61 prohibits the filing of a consolidated return; and we certainly think that the system followed by the department in trying to carry out the present bill should at least be permitted. If, under the definition of invested capital, these operating companies are limited to the par value of the stock, say \$6,000, with an 8 per cent return, which is \$480—

Senator JONES. Why do they put the capital stock at \$6,000?

Mr. THOMPSON. Just as a matter of convenience. That stock is not for the market. It was just organized because it was an operating company, and they turned in their property there, that is worth several thousand dollars, for that stock. It seems to me that invested capital should consist of money paid in and property paid in and of course valued as of the day of its transfer.

Senator PENROSE. Have you prepared an amendment?

Mr. THOMPSON. Yes, sir.

Senator PENROSE. Have you got it into the record?

Mr. THOMPSON. It is the amendment that Mr. Callbreath offered.

Senator THOMAS. We will consider it in that connection.

(The statement referred to above was presented by Mr. Thompson, and is here printed in full, as follows:)

JOPLIN-MIAMI MINING DISTRICT.

INVESTMENT AND EARNINGS OF 176 MINES REPRESENTATIVE OF THE ZINC INDUSTRY.

A committee was chosen by the Missouri-Oklahoma Zinc Mine Operators Association to present data pertaining to the earnings of zinc mines to the Treasury Department at Washington.

The aim of this committee has been to gather information from all mines in this district which have been productive during the past 20 years, especially those mines which have completed their record and have been mined out and abandoned; to tabulate the facts thus gathered and to make a truly representative statement of the investment made and the profits and losses resulting therefrom.

The figures herewith submitted are not represented as being exact statements from the books of the various mines; some of the companies for whose reports we have asked, had gone out of business and have no accessible records, but we have been able to obtain from their former owners statements of the capital invested and the profits and losses made which were certified to as being substantially correct, and the committee believe, from their own experience, that the aggregate of these statements constitutes a very accurate view of the history of the district.

This list does not include the thousands of prospects, which were drilled and developed during the past 20 years and which failed to become productive mines, but which nevertheless have absorbed several million dollars of capital and were a necessary charge upon the mining industry.

The following pages will show in detail the name and location of each mine, the amount of capital invested, the years during which the property was operated, the amount of net profit or loss and the final disposition of the plant.

There is also given a summary of these figures wherein the aggregate and average investments, times of productivity and profits and losses are shown separately for Missouri and Oklahoma and the entire district.

In conclusion, the committee wishes to draw attention to the fact that the results shown antedate the recent advances in all mining costs; because of these advances the capital investment now required to develop and equip a mine is vastly greater than the average investment here shown.

At the present time, April, 1918, the zinc ore market is very depressed and about two-thirds of all the mills in the district are shut down because they can not be operated at a profit.

Respectfully submitted.

L. C. CHURCH, *Chairman.*
P. B. BUTLER,
TEMPLE CHAPMAN, .
T. J. FRANKS,
W. B. SHACKLEFORD,
J. F. ROBINSON,
VICTOR RAKOWSKY,
Committee.

JOPLIN DISTRICT (INCLUDING WEBB CITY AND NEIGHBORING CAMPS).

Name of company.	District.	Investment.	From—	To—	Time.	Profit.	Loss.	Remarks.
Braucher Mining Co.....	Leadville Hollow	\$30,000	1908	1904	1 year.....		\$10,000	Mill sold, \$3,000.
Savango Mining Co.....	Joplin.....	23,000	1905	1907	2 years.....		19,000	Mill sold, \$3,000.
Sumner Mining Co.....	Prosperity.....	22,000	1907	1908	1 year.....		4,400	Mill sold, \$1,800.
Gold Standard Mining Co.....	Joplin.....	2,000	1903	1904	do.....		18,000	Mill sold, \$2,500.
St. Joe Mining Co.....	do.....	35,000	1915	1904	do.....		12,000	Mill sold, \$20,000.
Williams Mining Co.....	do.....	50,000	1905	1909	4 years.....		40,000	Mill sold, \$4,000.
B. & H. M. Mining Co.....	do.....	50,000	1905	1910	5 years.....		48,000	Mill sold, \$2,000.
Roma. Coal. Mining Co.....	do.....	12,000	1909	1913	4 years.....		12,000	Do.
Powers M. M. Mining Co.....	Klondike.....	7,500	1911	1915	do.....		40,000	Mill sold, \$2,500.
Little Jewel Mining Co.....	do.....	8,000	1908	1917	9 years.....		30,000	Mill sold, \$3,000.
Chicago Mines Co.....	Joplin.....	125,000	1912	1917	5 years.....		225,000	Mill sold, \$1,000.
Dayton Mining Co.....	Galeana.....	40,000	1911	1913	2 years.....		25,000	Mill sold, \$25,000.
Shawnee Hill Mining Co.....	Duanweg.....	25,000	1916	.....	3 months.....		18,000	Mill sold, \$7,500.
Hartford No. 1 Mining Co.....	Thomas Station	11,000	1912	.....	5 months.....		17,000	Mill sold, \$7,000.
Little John Mining Co.....	Cave Springs.....	80,000	1917	1917	2 years.....		17,000	Mill sold, \$7,000.
Lehigh Mining Co.....	Joplin.....	33,000	1915	1904	5 years.....	\$15,000	10,000	Mill sold, \$2,500.
Lehigh Mining Co. No. 2.....	Lehigh.....	70,000	1899	1906	6 years.....		60,000	Mill sold, \$2,000.
Conrad Mining Co.....	do.....	8,000	1900	1906	6 years.....		22,000	Mill sold, \$11,000.
Thanksgiving Mining Co.....	Joplin.....	20,000	1915	1917	14 years.....		20,000	Mill sold, \$20,000.
Little John Mining Co.....	Porto Rico.....	110,000	1913	1917	4 years.....		3,500	Mill sold, \$3,000.
Bird Dog Tailing Co.....	Webb City.....	20,000	1915	1915	2 years.....	28,000	20,000	Do.
Lincoln Mining Co.....	Klondike.....	15,000	1900	1903	3 years.....		20,000	Mill sold, \$1,000.
Lincoln Mining Co. No. 2.....	do.....	17,000	1899	1900	1 year.....	275,000	17,000	Mill sold, \$1,100.
John Jackson Mining Co.....	do.....	9,000	1898	1908	10 years.....	20,000	8,000	Mill sold, \$1,200.
John Jackson Tailing Co.....	do.....	2,500	1906	1908	2 years.....			Mill sold, \$2,500.
Horse Shoe Mining Co.....	do.....	8,000	1907	1908	1 year.....			Mill sold, \$1,300.
Brooklyn Mining Co.....	Duanweg.....	7,500	1902	1904	14 years.....	72,000		Mill sold, \$16,000.
Irish Mining Co.....	Joplin.....	6,000	1902	1903	1 year.....	10,000		Mill sold, \$2,500.
Hurricane Mining Co.....	do.....	60,000	1910	1911	do.....		60,000	Mill sold, \$1,000.
Aberdeen Mining Co.....	Klondike.....	30,000	1912	1915	3 years.....		17,000	Mill sold, \$4,000.
Hudson Mining Co.....	Carthage.....	25,000	1903	1908	5 years.....	100,000		Mill sold, \$12,000.
Troop No. 4 Mining Co.....	Joplin.....	15,000	1906	1909	3 years.....		150,000	Mill sold, \$10,000.
Mary C. Mining Co.....	Prosperity.....	50,000	1915	1916	1 year.....		65,000	Burned, insurance \$8,000.
Seneca Mining Co.....	do.....	25,000	1914	1916	2 years.....	68,000		Mill sold, \$2,300.
Schoenber-Walton Mining Co.....	Webb City.....	38,000	1906	1914	8 years.....		40,000	Mill sold, \$5,700.
Rice Mining Co.....	Prosperity.....	32,000	1906	1907	1 year.....		24,000	Mill sold, \$2,000.
Anomo Mining Co.....	do.....	14,000	1916	1915	3 months.....		65,000	Mill sold, \$2,800.
Gordon Hollow Mining Co.....	Joplin.....	32,000	1913	1915	2 years.....		58,000	Mill sold, \$1,250.
Uncle Joe Mining Co.....	Webb City.....	37,000	1913	.....	8 months.....			Mill sold, \$900.
Little Jewel Mining Co.....	Joplin.....	4,800	1894	.....	do.....	40,700		Mill sold, \$12,000.
Cock Robin Mining Co.....	do.....	3,700	1895	1902	7 years.....	115,000		Mill sold, \$2,000.
McDonald Bros. Mining Co.....	Prosperity.....	32,000	1917	1918	1 year.....	900	4,000	
Trouble Mining Co.....	Joplin.....	7,000	1896	.....	6 months.....			

JOPLIN DISTRICT (INCLUDING WEBB CITY AND NEIGHBORING CAMPS)—Continued.

Name of company.	District.	Investment.	From—	To—	Time.	Profit.	Loss.	Remarks.
Ground Floor Mining Co.	Webb City.	\$35,000	1907	1906	6 years		\$35,000	Mil sold, \$15,000.
Little Scott Mining Co.	Chittwood.	6,000	1904	1902	1 year.		10,000	Mil sold, \$1,500.
Ashland-Wilkes Mining Co.	Bellville.	10,000	1900	1903	2 years.		8,000	Mil sold, \$2,000.
Red Rose Mining Co.	Badger.	20,000	1903	1909	6 years.	\$1,000		Burned.
Badger M. & M. Mining Co.	do.	40,000	1903	1913	14 years.	20,000		Mil sold, \$350.
Tamogamy Mining Co.	do.	6,000	1900	1903	2 years.		2,000	Caved in.
do.	Joplin.	35,000	1906	1908	do.		50,000	Mil sold, \$2,500.
Thornton Mining Co.	do.	12,500	1909	1910	1 year.	15,000		Burned.
Grand Central Mining Co.	Webb City.	18,000	1908	1910	2 years.	8,000		Mil sold, \$2,000.
M. T. & O. Mining Co.	Jackson Hollow.	40,000	1906	1908	do.	5,500		Mil sold, \$15,000.
Winfred E. Mining Co.	Duenweg.	40,000	1908	1909	1 year.		37,500	Mil sold, \$2,500.
Morning Hour Mining Co.	West Joplin.	36,000	1906	1909	3 years.			Mil sold, \$1,500.
Independence Mining Co.	Royal Heights.	15,000	1900	1903	do.	98,000		Mil sold, \$2,500.
Innovator Mining Co.	Prosperity.	20,000	1907	1908	1 year.		11,000	Mil sold, \$3,500.
McManamy & Aldrich M. Co.	Chittwood.	6,000	1896	1897	do.			Mil sold, \$2,500.
Sunflower Mining Co.	Galeana.	4,100	1894	1892	2 years.	143,000		Mil sold, \$1,600.
Nancy Lee Mining Co.	Tanyard Hollow.	11,500	1901	1903	2 years.	20,000		Burned.
Annie Rooney Mining Co.	Galeana.	12,000	1901	1903	2 years.	13,000		Mil sold, \$2,000.
Sharp M. & M. Co.	Joplin.	12,000	1896	1897	do.	30,000		Mil sold, \$2,000.
King Jack Mining Co.	Leadville Hollow.	6,000	1899	1907	8 years.	150,000		Mil sold, \$1,000.
Bell B. Mining Co.	do.	15,000	1900	1902	2 years.		40,000	Mil sold, \$2,000.
Scott L. & Z. Co.	do.	25,000	1901	1903	2 years.	20,000		Do.
Success Mining Co.	Tanyard Hollow.	25,000	1901	1903	2 years.		15,000	Mil sold, \$3,000.
Federated M. & M. Co.	Galeana.	30,000	1910	1912	do.		30,000	Mil sold, \$10,000.
Julius S. Mining Co. No. 1.	Lehigh.	24,000	1908	1912	4 years.	120,000		Burned.
Julius S. Mining Co. No. 2.	Need City.	12,000	1909	1912	3 years.	20,000		Mil sold, \$1,800.
Walker Mining Co.	Alba.	12,000	1907	1908	1 year.		25,000	Mil sold, \$2,500.
Albert F. Mining Co.	Prosperity.	15,000	1908	1912	4 years.		8,000	Mil sold, \$1,400.
Geo. H. Mining Co.	do.	20,000	1905	1912	7 years.	20,000		Mil sold, \$2,500.
Emms S. Mining Co.	do.	24,000	1907	1912	5 years.	45,000		Mil sold, \$2,500.
William F. Mining Co.	do.	24,000	1907	1912	5 years.	160,000		Do.
Louis F. Mining Co.	Duenweg.	12,000	1906	1908	2 years.		20,000	Mil sold, \$1,200.
Peacock Mining Co. No. 2.	Bell Center.	12,000	1906	1908	2 years.		15,000	Mil sold, \$1,500.
Peacock Mining Co. No. 1.	do.	20,000	1906	1909	3 years.		30,000	Mil sold, \$5,000.
Yellow Pup Mining Co.	Peacock.	32,000	1900	1917	17 years.	175,000		Mil sold, \$1,000.
Abedin L. & Z. Co.	do.	12,000	1902	1917	15 years.	60,000		Mil sold, \$10,000.
La Paloma Z. Co.	Spring City.	4,000	1908	1908	2 years.		35,000	Mil sold, \$5,000.
Green Point Z. Co.	Spring City.	7,000	1908	1908	1 year.		8,000	Abandoned.
White Oak Mining Co.	Galeana.	19,000	1909	1900	do.		19,000	Caved.
Chicago Z. Co.	Tipple Ford.	31,000	1914	1916	2 years.		27,000	Mil sold, \$2,250.
Leadville Hollow Mining Co.	Leadville Hollow.	25,000	1900	1901	1 year.		27,000	Mil sold, \$1,000.
Willcox Mines Co.	do.	18,000	1900	1901	do.		24,000	Mil sold, \$2,200.
Chapman & Lennan Mining Co.	Chittwood.	28,000	1910	1911	do.		38,000	Mil sold, \$4,000.
Webb City.	Webb City.	40,000	1904	1905	do.	5,000		Do.

Name of mines	Investment.	From—	To—	Time operated.	Profit.	Loss.	Even.	Do.
Mount Anarat Mine.	30,000	1903	1904	do.				Do.
New Atlas Mining Co.	26,000	1901	1905	6 months.			25,000	Do.
Alexandra Mining Co.	30,000	1901	1905	21 years.			30,000	Do.
Pinger Mining Co.	50,000	1906	1909	3 years.			31,000	Burned.
Newbern Mining Co.	40,000	1908	1910	10 months.				Moved.
Red Dog Mining Co.	52,000	1907	1910	3 years.			28,000	Mill sold.
Bull Dog Mining Co.	47,000	1908	1909	14 years.				Burned.
Little Mary Mining Co.	80,000	1909	1913	4 years.			50,000	Removed.
Lougarre-Chapman Mining Co.	56,250	1913	1917	do.			309,300	Mill sold.
Silver Hollow Mining Co.	185,000	1904	1905	8 months.			120,000	Mill sold.
Rice Mining Co.	25,000	1905	1906	1 year.			20,000	Removed.
Eliza Mining Co.	35,000	1905	1906	3 months.			32,000	Do.
Bessie Mining Co.	20,000	1905	1906	15 months.			20,000	Do.
Superior Mining Co.	25,000	1905	1906	10 months.			20,000	Do.
Big Reuben Mining Co.	25,000	1906	1907	do.		5,000		Do.
Cornfield Mining Co.	20,000	1905	1907	15 months.			15,000	Do.
Mosely Mining Co.	35,000	1905	1906	12 months.			25,000	Do.
Franklin Mining Co.	60,000	1906	1907	15 months.			65,000	Do.
Premier Mining Co.	25,000	1907	1908	8 months.			20,000	Do.
Ben Nevis Mining Co.	60,000	1907	1908	15 months.			53,000	Do.
111 mines.	3,220,850			286 years.		2,590,400	2,329,400	

MIAMI DISTRICT (INCLUDING COMMERCE AND LINCOLNVILLE CAMPS).

Name of mines	Investment.	From—	To—	Time operated.	Profit.	Loss.	Remarks.
Old Chief.	\$30,000.00	1908	1917	7 years.	\$34,000.00		Mill burned.
Sullivan.	35,000.00	1909	1917	4 years 4 months	28,354.80		Mill idle.
Buckeye.	25,000.00	1908	1917	5 years 4 months	30,000.00		Still operating.
Joplin-Miami.	5,000.00	None.	None.	None.		\$5,000.00	No mli.
Lawson.	30,000.00	1909	1910	1 year.		15,000.00	Mill removed.
Midas.	35,000.00	1912	1917	3 years 5 months			Do.
Crescent.	20,000.00	1909	1910	11 months.	10,000.00		Mill sold and removed.
Southern Queen.	20,000.00	1910	1910	5 months.		15,000.00	Do.
Oklmulgee.	15,000.00	1909	1910	6 months.		12,000.00	Mill removed.
Red Bird.	15,000.00	1909	1910	5 months.		10,000.00	Do.
Golden Hen.	30,000.00	1909	1916	1 year 4 months.		25,000.00	Do.
Miami Yankee.	25,000.00	1910	1916	8 months.		35,000.00	Do.
Little Yankee.	35,000.00	1911	1913	2 years.			Mill sold under mortgage.
Neverwest.	10,000.00	1913	1916	2 years 11 months.	32,000.00		Mill idle.
Consolidated.	30,000.00	1911	1912	1 year.		15,000.00	Mill removed.
Cactus No. 2.	25,000.00	1915	1917	2 years.		21,701.83	Still operating.
Turkey Fat.	15,000.00	1908	1917	8 years.	337,285.00		Mill idle.
New State.	40,000.00	1908	1916	7 years 6 months.	68,000.00		Mill removed.
Index-Mispa.	50,000.00	1909	1917	6 years.	15,000.00		Do.
Swastika.	40,000.00	1909	1910	1 year.		12,000.00	Do.
Cactus No. 1.	50,000.00	1913	1915	2 years.		55,000.00	Do.
Commonwealth.	15,000.00	1911	1912	8 months.		10,000.00	Do.

MIAMI DISTRICT (INCLUDING COMMERCE AND LINCOLNVILLE CAMPS)—Continued.

Name of mines.	Investment.	From—	To—	Time operated.	Profit.	Loss.	Remarks.
Eureka.....	\$25,000.00	1912	1915	1 year.....	\$84,000.00	\$15,000.00	Mill idle.
Lost Trail.....	32,000.00	1913	1917	3 years 8 months.....			Do.
Wau Hillau.....	20,000.00	1911	1912	1 year 4 months.....		15,000.00	Mill removed.
Emma Gordon.....	50,000.00	1909	1917	8 years.....	25,800.00		Mill idle.
Prarie.....	75,000.00	1914	1917	3 years.....	20,000.00		Still operating.
King Jack.....	20,000.00	1909	1917	7 years.....	88,000.00		Mill removed.
Vantage.....	50,000.00	1914	1916	2 years.....	35,000.00		Do.
Gray Top.....	40,000.00	1912	1913	6 months.....		40,000.00	Mill sold, \$5,600.
McCannell-Harnes.....	40,000.00	1914	1916	2 years.....	125,000.00		Mill removed.
Carson-Podson.....	80,000.00	1912	1913	1 year.....		70,000.00	
Thirty Acre.....	40,000.00	1912	1914	2 years.....		35,000.00	
Oklahoma L. & Z. Co.....	55,000.00	1912	1913	do.....		50,000.00	
Carson Mfg. Co. (2).....	90,000.00	1914	1917	4 years.....	200,000.00		1 mill removed, 1 idle.
Pack Horse.....	15,000.00	1906	1909	3 years.....		12,000.00	Mill burned down.
Hannibal.....	20,000.00	1910	1912	2 years.....		20,000.00	Recently started up.
Johanna.....	15,000.00	1908	1910	do.....	8,000.00		Mill sold and removed.
Perkins.....	25,000.00	1908	1911	3 years.....		25,000.00	Mill removed.
Kat's, or M. K. & T.....	30,000.00	1908	1908	2 years.....		30,000.00	Do.
Big Jack.....	250,000.00	1909	1912	3 years.....		250,000.00	Creditors got 50 per cent.
F. F. F.....	9,000.00	1908	1909	1 year.....		5,000.00	Mill removed.
Red Feather.....	50,000.00	1910	1912	2 years.....		5,000.00	Sublessees also lost.
Petersburg.....	50,000.00	1909	1917	8 years.....		50,000.00	Operated intermittently.
Diamond C.....	50,000.00	1909	1910	1 year.....		50,000.00	Mill removed.
Hobo.....	12,000.00	1909	1912	3 years.....	10,000.00		Do.
Heip O'Brien.....	40,000.00	1909	1912	do.....		30,000.00	Do.
New Landis.....	50,000.00	1910	1911	1 year.....		50,000.00	Do.
Old Abe.....	75,000.00	1907	1912	5 years.....		75,000.00	Do.
Lucile.....	40,000.00	1908	1911	2 1/2 years.....		40,000.00	Do.
Good Luck.....	10,000.00	1909	1912	do.....	10,000.00		Do.
McAulter.....	18,000.00	None.	None.	1 year.....		18,000.00	Mill sold for taxes, 1909.
Rush & Elder.....	6,000.00	1907	1908	1 year.....		6,000.00	Mill removed.
Mason.....	75,000.00	1908	1910	2 years.....		75,000.00	Do.
Virginia.....	15,000.00	None.	None.	do.....		15,000.00	Do.
Oklahoma.....	150,000.00	1909	1909	6 months.....		35,000.00	Mill sold for taxes.
Lancaster.....	25,000.00	1908	1909	1 year.....		15,000.00	Mill burned.
Chicago-Quapaw.....	20,000.00	1909	1910	1 year.....		20,000.00	Mill removed.
Nunny Side.....	40,000.00	1907	1910	3 years.....		15,000.00	Do.
White Eagle.....	40,000.00	1908	1911	do.....		40,000.00	Mill idle.
Lincolnville.....	10,000.00	1907	1908	6 months.....		10,000.00	Mill removed.
Quincy.....	15,000.00	None.	None.	do.....		15,000.00	Do.
Myrtle.....	25,000.00	1909	1910	1 year.....		25,000.00	Do.
64 mines.....	2,375,000.00			153 years.....	1,162,441.80	1,416,791.83	

GENERAL SUMMARY.

JOPLIN DISTRICT (INCLUDING WEBB CITY AND NEIGHBORING CAMPS).

Successful (38 mines):	
Total invested.....	\$910,850
Average invested.....	24,000
Total time operated, 162 years.	
Average time operated, 4½ years	
Total profit.....	2,590,400
Average profit.....	68,150
Unsuccessful (73 mines):	
Total invested.....	2,310,000
Average invested.....	31,600
Total time operated, 134 years.	
Average time operated, 1½ years.	
Total loss.....	2,329,400
Average loss.....	31,900
Summary (111 mines):	
Total invested.....	3,220,850
Average invested.....	29,000
Total time operated, 296 years.	
Average time operated, 2½ years	
Net profit.....	261,000
Average profit.....	2,350

MIAMI DISTRICT (INCLUDING COMMERCE AND LINCOLNVILLE CAMPS).

Successful (19 mines):	
Total invested.....	\$637,000
Average invested.....	33,500
Total time operated, 81½ years.	
Average time operated, 4½ years.	
Total profit.....	1,162,400
Average profit.....	61,100
Unsuccessful (45 mines):	
Total invested.....	1,738,000
Average invested.....	38,622
Total time operated, 71½ years	
Average time operated, 1½ years	
Total loss.....	1,416,000
Average loss.....	31,484
Summary (64 mines):	
Total invested.....	2,375,000
Average invested.....	37,000
Total time operated, 153 years.	
Average time operated, 2½ years.	
Net loss.....	254,400
Average loss.....	3,974

ENTIRE JOPLIN-MIAMI DISTRICT.

Successful (57 mines):	
Total invested.....	\$1,547,850
Average invested.....	27,150
Total time operated, 243½ years.	
Average time operated, 4½ years.	
Total profit.....	3,752,800
Average profit.....	65,700
Unsuccessful (118 mines):	
Total invested.....	4,048,000
Average invested.....	34,000
Total time operated, 205 years.	
Average time operated, 1½ years.	
Total loss.....	3,746,200
Average loss.....	31,000
Summary (175 mines):	
Total invested.....	5,595,850
Average invested.....	32,000
Total time operated, 449 years.	
Average time operated, 2½ years.	
Net profit.....	6,600
Average profit.....	37

Senator THOMAS. Mr. Maloney, I understand that you are obliged to go back to New York to-day.

Mr. MALONEY. I will say that with your permission this afternoon will be perfectly satisfactory. The only object I have in going back to New York is to register for the draft.

Senator PENROSE. We can hear you now.

Senator THOMAS. How long will you desire to speak?

Mr. MALONEY. Ten or fifteen minutes. I desire to speak for Thomas B. Maloney, L. B. Wilson, and R. Tracy Falk.

STOCKS AND BONDS.

**STATEMENT OF MR. T. B. MALONEY, 32 BEAVER STREET,
NEW YORK CITY.**

Senator PENROSE. What position do you occupy on the stock exchange?

Mr. MALONEY. I am a member of the Consolidated Stock Exchange of New York, and we are here to call your attention to section 1107, Schedule A, paragraph 4. That is in reference to the transfer tax on the sale of stocks and bonds, and also on borrowing and loaning stocks.

I wanted to confine my remarks entirely to the tax on loans, eliminating entirely the tax on the transfer and sale of stocks.

This section which we are operating under, or which the Treasury Department now enforces, was enacted in the law of last year which went into effect in December. There was no attempt made to collect this tax whatever from December until March, by the Internal Revenue Department, and those engaged in this occupation had no idea that there was such a thing as a tax on loans or borrowed stock among members, and the Treasury Department, or the Internal Revenue Department, due to the fact that they had not made any attempt to collect the tax during the four months, were of the same opinion. Again, the Treasury Department in sending out their printed forms of instructions and the like made no reference whatever to the collection of this tax on stock loaned or borrowed.

The Attorney General has rendered an opinion that stocks loaned and borrowed among members of exchanges are taxable, although loans made with banks are not taxable; and the substance of his opinion is this, that we go to a bank and borrow money. You make a loan among the members yourself, and you borrow the stock. That is his interpretation of the law. We feel that that has been a very great handicap in the conduct of the business, to begin with. It means that the loaning and borrowing of stock among members themselves has been practically eliminated owing to the fact that this tax is enforced, and we can go to the banks where we pay no tax. That adds an additional burden on the money market and an additional burden on the banks, because the taxes are so heavy that to eliminate them we have got to go to the banks.

I call your attention, also, to the fact that the stamp tax is practically an adoption of the New York law. That is the original idea in New York, and although the Federal law does not follow the New York law literally, the substance is the same. There is no mention made in the New York law; in fact, loans and borrowings of stock are expressly exempt. They specify it in that law.

I wanted to call your attention to a concrete example of the operation of this tax on stocks loaned and borrowed.

We will take a client living in San Francisco who wires his broker in New York to sell a hundred shares of Erie Railroad stock at \$15 a share, and notifies him that he will mail the certificate. In the communication he says, "I will send this certificate of stock to you by mail." The broker, on receiving his instructions to sell it, sells immediately. He must wait days before he can actually receive the certificate of stock from his client. From the day he sells that stock

until the day the certificate is delivered, that broker is technically short 100 shares of Erie Railroad stock which he must borrow until he receives the certificate. He must borrow this stock on the day that it is sold to deliver it to the man who has purchased it from him. He must repeat that operation for five or six days, and every time he does it he pays a tax of \$4 although he is waiting for the receipt of that certificate.

Senator THOMAS. Why must he repeat it so frequently?

Mr. MALONEY. Because loans are usually returned the day after loans are made. From day to day, if he can find somebody that will make a loan, then he will only have to pay \$4.

Senator THOMAS. That is an exchange regulation?

Mr. MALONEY. No; that is the convenience of the man for whom he buys the stock.

Senator THOMAS. The custom?

Mr. MALONEY. The other broker has sold his stock. The next day he calls that loan. So it is liable to operate every day until that certificate is received.

Senator NUGENT. That is merely a custom that is in vogue among brokers?

Mr. MALONEY. It is a system of purchase and sale. If I have a hundred shares of stock and a man wants to borrow it I say, "I will loan it to you." If to-morrow I can sell at a good price I sell that stock out, and then I call that back.

Senator THOMAS. Did you appear before the Ways and Means Committee?

Mr. MALONEY. No, sir; we did not have an opportunity because we did not have any idea what the bill was going to be this year. We got there so late that they were taking up other things, and we did not attempt to get a hearing.

I want to say here and now that we have hesitated about doing it, because we do not want to appear as asking for a reduction of any tax that we thought the Government had intended to collect.

Senator THOMAS. Now, Mr. Maloney, I think I can speak for the committee when I say that we are glad to hear you. We want information, and the only way to get it is to get it from those who are affected by the provisions of the bill and whose information regarding that particular subject is better than ours probably is or will be.

Mr. MALONEY. I can speak for my own exchange in saying that we have no objection to the taxes levied now. We are satisfied with them, because we know the United States needs the money. I myself have sat on legislative committees when I was a member of the Legislature of New York, and I know what the committee has to contend with.

That man, as the law requires, pays \$2 when he sells that 100 shares of stock. That is all the law requires of him when he sells it. That is all the law says he shall pay. But, nevertheless, he actually pays \$22 to sell a hundred shares of stock, because he can not deliver the certificate in time; it is too far away. That \$4 tax must be paid every time he borrows or loans his stock—

Senator PENROSE. Have you prepared any amendment to cover the phraseology?

Mr. MALONEY. Yes, sir; I can cover it in about four words which the New York statute has.

Senator PENROSE. Get that into the record.

Mr. MALONEY. It is in this brief.

Senator PENROSE. Get it into the record so that we will have a note of it.

Mr. MALONEY. We suggest that it be amended by using the following words: "nor upon mere loans of stock or the return thereof."

Senator PENROSE. Where would you put that in?

Mr. MALONEY. That would go in paragraph 4, after the words "deliver or transfer for such purpose of certificates so deposited."

I am coming, now, to the question of the effect of this operation on the money situation.

Another illustration is that of a broker having a loan with a bank, the collateral of which is made up of industrial and railroad stocks. A certain proportion of railroad stocks and all 100-share lots secures a lower interest rate on the entire loan, and in fact, banks really insist upon 100-share lots of any particular stock.

Part of this required minimum of railroad stocks is 100 shares of Erie. If 50 shares are sold on order, the broker is unable to withdraw 50 shares from his loan, so must borrow this 50 shares sold until his client sells the other 50 shares, and, under the opinion of the Attorney General, is required to pay a tax on the borrowed and returned stock for an indefinite period; not a tax at the rate of \$2 per 100 shares on the sale as the law requires, but a much larger sum, the tax being equivalent to 96 per cent for 1 day in the case of Erie, 64 per cent in the case of Missouri Pacific.

Such cases, called borrowing and loaning of stock, are in reality the exact opposite. It is the money that is borrowed and loaned. The average price of all stock listed on the exchange today is about \$60 per share. At the prevailing money rate of 6 per cent, the tax on loans is equivalent to 24 per cent a day.

Another illustration: A broker received an order a minute before the close of the market to sell 100 shares of stock, and, physically unable to call the 100 shares from a broker he may have it loaned to, before the close, he must borrow the stock for one day, and thereby pay a tax of \$4, thereby making the tax on the sale of 100 shares of stock \$6 instead of \$2, as required by law. This tax prevents carrying of stocks by those with spare capital for others who are willing to lend them and requires the borrowing of money from banks, thereby placing an unnecessary demand on the money market.

There has been some doubt in the minds of those engaged in this occupation as to the correctness of the Attorney General's opinion, but of course this law is, in effect, operating under the opinion of the Attorney General. We have considered it unpatriotic to try this case in court, and we have shouldered all the tax with the idea in mind that in the new bill to be adopted this year Congress would clearly exempt borrowed and loaned stocks from the tax. We do not ask remission of any tax producing any material revenue, nor the annual tax on brokers. We do ask for the removal of the existing uncertainty under which a ruling has been made bringing in very little revenue at the expense of great inconvenience and hardship in our daily transactions and one which we believe was not the intention of Congress to impose.

Senator THOMAS. Have you a copy of that ruling?

Mr. MALONEY. Yes, sir; I have it here.

Senator THOMAS. Would you put it in the record, please?

Mr. MALONEY. I will make a copy of this and submit it to the stenographer.

Senator THOMAS. You can do that and send it to the stenographer.

Mr. MALONEY. Yes, sir; I will do that this afternoon.

(The brief referred to above is here printed in full, as follows:)

DEPARTMENT OF JUSTICE,
Washington, March 23, 1918.

The SECRETARY OF THE TREASURY.

SIR: I have the honor to acknowledge your letter of the 14th instant requesting my opinion on the question whether the stamp tax imposed by sections 800 and 807, schedule A, subdivision 4, of Title VIII, of the war-revenue act of October 3, 1917 (40 Stat., 319, 322), applies to the so-called borrowing and return of shares of certificates of stock.

The said subdivision levies a tax "on all sales, or agreements to sell, or memoranda of sale or deliveries of or transfers of legal title to shares or certificates of stock * * * whether made upon or shown by the books of the association, company, or corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock or not * * * : *Provided*, That it is not intended by this title to impose a tax upon an agreement evidencing a deposit of stock certificates as collateral security for money loaned thereon which stock certificates are not actually sold, nor upon such stock certificates so deposited: *Provided further*, That the tax shall not be imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased same * * *."

Your letter makes the following further statement:

"The transactions as to which the question arises are described as follows:

"The borrowing of shares is necessary in connection with all so-called short sales. It is also necessary in connection with shares that are sold but are not on hand for delivery, an instance of which is the shares being in transit from abroad or the West, or elsewhere. It also frequently happens that a broker may sell shares for an estate and find upon attempting to transfer them from the name of a decedent or an executor that additional papers, or authority, are required by the transfer office, or the transfer books may be closed for a meeting of stockholders or other reasons, and the shares being already sold the broker borrows to make delivery, after replacing the borrowed shares.

"In the case of the short-sale transaction the following occurs:

"A sells to B 100 shares of stock which is evidenced by memorandum of sale. Under the rules of the exchange the shares have to be delivered and paid for the day following. If the sale is a short sale or the shares are not on hand for delivery, A applies to C, who has such shares on hand, for a loan of them. C being willing to lend them delivers to A a certificate for 100 shares indorsed in blank on A's agreement to redeliver to him an equivalent number of shares on demand on any business day and the deposit by A with C of the market value of the shares as security for their return. That deposit remains until the shares are returned, subject to increase from day to day if the market value of the shares rises, and to decrease from day to day if the market value of the shares falls. A makes his delivery under his transaction with B by delivering the certificate which he has borrowed from C for that purpose, thereby completing the transaction between A and B on which the tax is paid. When A desires to return the shares which he has borrowed, A goes into the market and buys 100 shares for the purpose of delivering them to C, and on that transaction the tax is paid. These shares so acquired for delivery to C he delivers to C and receives the amount he has on deposit with C. It is a common occurrence that C demands the return of his shares in which event A substitutes D as another lender, going through the same process, including the deposit of the value of the shares, as with C, thus delivering to C the shares he has borrowed from D for that purpose, and receiving from C the amount on deposit with him as security for such return. This process may be repeated many times in respect of the same short sale.

"The stamp tax provided for in the subdivision above quoted of course applies to the sale and delivery of any borrowed shares and to the purchase of shares for the purpose of returning them to a lender. The precise question

upon which opinion is desired is as to whether the stamp tax also applies to the passing from the lender to the borrower of the shares or certificates of stock 'borrowed' and also to the passing from the borrower to the lender of shares or certificates of stock 'returned.'"

You inclose a copy of an opinion rendered you by the Solicitor of Internal Revenue to the effect that the transfer of the stock from the lender to the borrower, and later from the borrower to the lender in fulfillment of the former's obligation, are both subject to the tax. With this conclusion I agree for the following reasons:

1. The act by its express terms, it will be observed, covers every transfer of the legal title to shares of stock with certain specific exceptions. There can certainly be no doubt that there is a transfer of the legal title from the lender to the borrower and later from the borrower to the lender under the circumstances stated. Shares of stock are fungible things, and their loan with an agreement to return things of the same class is the *mutuum* of Roman law, as to which no one can doubt that title passes from the lender to the borrower and vice versa. (Jones on Pledges, p. 64; Story on Bailments 7th ed., secs. 283, 284; Kent's Commentaries, 12th ed., Vol. II, p. 573; Hurd v. West, 7 Cowen (N. Y.) 752, 756). Even if the article be mingled with others of the same species in a warehouse, title may pass to the warehouseman. (Kent's Commentaries, 12th ed., Vol. II, p. 590. Justice Himes' note; South Australian Ins. Co. v. Randell, L. R., 3 Privy Council Appeals 101; Rahilly v. Wilson, 3 Dillon 420.) Upon the same principle title to deposits in bank passes to the banker. (Foley v. Hill, 2 House of Lords, (cas. 28.) The Supreme Court has had occasion to pass upon this characteristic of shares of stock in several cases. (Richardson v. Shaw, 209 U. S. 365; Sexton v. Kessler, 225 U. S. 90; Gorman v. Littlefield, 229 U. S. 19; National City Bank v. Hotchkiss, 231 U. S. 50; Duel v. Hollins, 241 U. S. 523; and see as to bonds United States and Mex. T. Co. v. Kansas City, M. & O. Ry. Co., 240 Fed. 505.) In Gorman v. Littlefield, the court held:

"* * * That a certificate for the same number of shares represented precisely the same kind and value of property as another certificate for a like number of shares in the same corporation; that the return of a different certificate or the substitution of one certificate for another made no material change in the property right of the customer; that such shares were unlike distinct articles of personal property, differing in kind or value, as a horse, wagon, or harness, and that stock has no earmark which distinguishes one share from another, but is like grain of a uniform quality in an elevator one bushel being of the same kind and value as another * * *"

The effect of these decisions is undoubtedly that even in the case of a broker and his customer the legal title to the stock is, not nominally, but really in the broker, if the course of business so requires, although the customer may retain, as against the broker and his trustee in bankruptcy, an equitable right in rem to stock in the broker's possession of the same species as that dealt in between them.

In accordance with this same general principle, it is specifically held that a loan of stock transfers title (Dykens v. Allen, 7 Hill (N. Y.) 497; Barclay v. Culver, 30 Hun (N. Y.) 1; Fosdick v. Greene 27 Ohio St., 484, Dos Passos on Stockbrokers, 2d. p. 329.)

2. It can not be said that the borrower is a mere agent between the lender and the vendee, so as to make what is in appearance two transactions in reality only one. There is no privity between the lender and the vendee. The former looks merely to the borrower and assumes no relationship further. There are, therefore, in substance, two transactions, a transfer by the lender to the borrower, and a transfer by the latter to the vendee, and the tax must be paid on each. The case, in this aspect of it, is governed by Metropolitan Telegraph & Stock Co. v. Ward, 133 Fed. 70, affirmed 138 Fed. 1000, and Eldridge v. Ward, 174 Fed. 402, and not by United States v. Clawson, 119 Fed. 904; Metropolitan Stock Exchange v. Gill, 190 Fed. 545, S. C. 211 Fed. 108, and Board of Trade v. Hammond Elevator Co., 198 U. S. 424.

3. As for the provisos in subdivision 4, they should receive a fair interpretation in connection with the whole, but there must be clear language before it can be assumed that exemption from taxation was intended. (Cornell v. Coyne, 192 U. S., 418, 431; Ford v. Delta & Pine Land Co., 164 U. S., 662, 690; Central Railroad & Banking Co. v. Georgia, 92 U. S., 665, 674; Bailey v. Magwire, 22 Wall., 215, 226.) The first proviso deals with deposits of stock as collateral security for a loan, and the second with the transfer of stock between a broker

and his customer. Under no fair interpretation can either be held to cover the loan of stock under the circumstances now under consideration.

A loan of stock can not be called a pledge thereof within the meaning of the first proviso. The transaction is, in effect, the reverse of that covered by the proviso. In the latter case money is loaned and stock is deposited as collateral for its return. In the case now in question stock is loaned and money is deposited as collateral for its return. In one case the debt is money, in the other stock. (See *Dibble v. Richardson*, 171 N. Y., 131, 137.) There can, of course, be no doubt that the legal title to the money loaned passes in a real sense in the case covered by the proviso, and for the same reason legal title to the stock loaned in the present case passes with like reality to the borrower.

As to the second proviso, it is sufficient to say that the relationship between the lender and the borrower in the present case is not, in any sense, that of a broker buying and selling stocks for a customer.

Respectfully,

JOHN W. DAVIS,
Acting Attorney General.

MR. MALONEY. If this tax produced quite a revenue, of course you ought to continue to have it. As a matter of fact it does not produce any revenue at all. For the first four months of the year it did, because we were not aware of this tax during the months of December, January, February, and March, and the Internal-Revenue Department collected and made it retroactive to December and collected a lump sum from everybody who had these loans, and it produced quite a revenue for four months. But since that the operation of it has been such that practically there is no revenue now being derived from this tax by the Government, and it is placing a hindrance on the operation of the business and it has forced borrowers to go to banks. There does not seem to be any difference, in my mind, if I go to a man and say, "Have you got a hundred shares of Union Pacific Railroad stock?" and he says, "Yes." He lets me have it. I borrow it. I am responsible for the value of the stock, but I can go to the bank and get it at 6 per cent. I must pay him not only the prevailing rate of interest, but \$4 as well. If we were permitted to borrow among ourselves, among the men who are members of the stock exchange and who have capital and were willing to loan it, it would relieve the banks of an embarrassing situation which is going to become worse instead of better.

All trades that go through our clearing house, according to the interpretation of the Attorney General, are taxable, although the same operation may go through a bank and is not.

As I say, if it were producing a great amount of income or revenue to the Government, we would hesitate very much about coming here and asking for any reduction in the tax, but we know from our own experience in the business that it does not produce anything. I doubt if it runs up into six figures for the entire year.

We feel that we are not asking to deprive the Government of any tax which they ever expect to collect.

I will file this brief with you, Mr. Chairman, and I might also say, in closing, that I have a telegram from a member of the Boston exchange which says he was unable to get here, but is "in hearty sympathy with your contention."

Senator THOMAS. Mr. Maloney, I presume you speak for all the exchanges?

Mr. MALONEY. I do not speak for the New York Stock Exchange, but, indirectly, for the business in general.

There was another matter that I wanted to bring up before this committee, but I was unable to secure the exact information from the Internal-Revenue Department. Judge Graham informs me that most likely they would have it in a day or so——

Senator THOMAS. We will probably extend these hearings for several days.

Mr. MALONEY. It is in reference to the question of this tax on the transfer of stocks. As it is to-day, the Government will most likely get a little over \$5,000,000 out of it. Six or seven hundred men pay 50 per cent of that tax—over \$2,000,000—which is an average of about \$8,000 a year tax. That is not a tax on their profits; it is a tax on their losses as well, and we had a suggestion which we wanted to offer——

Senator THOMAS. You can offer that when you get your further information.

Senator PENROSE. Would you like another hearing?

Mr. MALONEY. Yes, sir.

Senator PENROSE. You can get it whenever you want.

Senator NUGENT. Do I understand you to say that the revenue derived by the Government would run into six figures?

Mr. MALONEY. I doubt if it will. As a matter of fact, Senator, the form with which the Internal Revenue Department supplied us——

Senator NUGENT. What do you mean by six figures?

Mr. MALONEY. A hundred thousand dollars; but I doubt if it would be \$50,000, because that is practically eliminated entirely. The Government will not lose anything; otherwise we would not be here.

(Mr. Maloney thereupon submitted a brief, which is here printed in full, as follows:)

CONSOLIDATED STOCK EXCHANGE OF NEW YORK,
President's Office, September 11, 1918.

TO COMMITTEE ON FINANCE, UNITED STATES SENATE:

Section 1107, schedule A., paragraph 4 (pp. 164-165) of the proposed revenue law, has been interpreted by the Attorney General, in an opinion to the Commissioner of Internal Revenue, to hold that loans on borrowed stock and return loans are taxable the same as sales of stock.

We are of the opinion that it was not the intention of Congress to impose this tax nor did the Internal Revenue Department expect to collect such a tax, for the following reasons:

First. When this act became effective, December 1, 1917, the Internal Revenue Department issued instructions and had printed forms prepared which were distributed to those engaged as dealers in securities and no mention was made of nor any attempt made to collect this tax. The matter came to the attention of the department and an opinion was rendered by the Attorney General, March 23, 1918, holding that stocks borrowed, loaned and returned, were taxable. We call your attention to the fact that almost four months elapsed before any attempt was made to collect this tax.

Second. This section was based on the New York statute, which does not impose this tax.

The borrowing and loaning of stock is necessary in connection with shares sold but not on hand for immediate delivery, an instance of which is the shares being in transit from abroad or the West or from some distant point. It also frequently happens that a broker may sell shares for an estate and that certain papers are required to insure valid title to the stock or that the transfer books are closed. The stock being sold, the broker must borrow the stock to make delivery. The actual operation of the tax on stocks loaned or borrowed is as follows:

A client living in San Francisco wires his broker in New York to sell 100 shares of Erie Railroad common stock at \$15 a share and notifies him that he will mail the certificate. The customer pays \$2 tax on sale. The broker must

borrow the stock to make delivery to the purchaser. The loaner calls the stock back the next day. The customer pays a \$2 tax on the loan and \$2 additional when the stock is returned—\$4 in all. This operation continues for a period of six days, until the certificate is received from San Francisco. Instead of \$2 tax on the sale of 100 shares, as the law directs, he would pay \$22.

Another illustration is a broker having a loan with a bank, the collateral of which is made up of industrial and railroad stocks. A certain proportion of railroad stocks and all 100-share lots secures a lower interest rate on the entire loan. Part of this required minimum of railroad stocks is 100 shares of Erie. If 50 shares is sold on order, the broker is unable to withdraw 50 shares from his loan, so must borrow this 50 shares sold until his client sells the other 50 shares, and, under the opinion of the Attorney General, is required to pay a tax on the borrowed and returned stock for an indefinite period, not a tax at rate of \$2 per 100 shares on the sale as the law requires, but a much larger sum, the tax being equivalent to 96 per cent for one day in the case of Erie, 64 per cent in the case of Missouri Pacific, etc. Such cases, called borrowing and loaning of stocks, are in reality the exact opposite. It is the money that is borrowed and loaned. The average price of all stock listed on the exchange to-day is about \$60 per share. At the prevailing money rate of 6 per cent, the tax on loans is equivalent to 24 per cent a day.

Another illustration: A broker received an order a minute before the close of the market to sell 100 shares of stock and, physically unable to call the 100 shares from a broker, he may have it loaned to, before the close, he must borrow the stock for one day and thereby pay a tax of \$4, making the tax on the sale of 100 shares of stock \$6, instead of \$2, as required by law.

This tax prevents carrying of stocks by those with spare capital for others who are willing to lend them and requires the borrowing of money from banks, thereby placing an unnecessary demand on the money market.

There has been some doubt in the minds of those engaged in this occupation as to the correctness of the Attorney General's opinion, but to test the question in court has been considered unpatriotic and we have shouldered the tax with the idea in mind that, in the bill to be adopted this year, Congress would clearly exempt borrowed and loaned stock from the tax. We do not ask remission of any tax producing any material revenue nor the annual tax on brokers. We do ask for a removal of the existing uncertainty under which a ruling has been made bringing in very little revenue at the expense of great inconvenience and hardship in our daily transactions and one which we believe was not the intention of Congress to impose. We respectfully would suggest that the New York statute be followed in this respect, so that section 1107, schedule A, paragraph 4, include clearly in the exemption "nor upon mere loans of stock and the return thereof," read as follows:

"Capital stock, sales or transfers: On all sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares or certificates of stock or of profits or of interest in property or accumulation in any corporation, or to rights to subscribe for or to receive such shares or certificates, whether made upon or shown by the books of the corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not, on each \$100 of face value or fraction thereof, 2 cents, and where such shares are without par or face value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share, unless the actual value thereof is in excess of \$100 per share, in which case the tax shall be 2 cents on each \$100 of actual value or fraction thereof: *Provided*, That it is not intended by this title to impose a tax upon an agreement evidencing a deposit of certificates as collateral security for money loaned thereon, which certificates are not actually sold, nor upon the delivery or transfer for such purpose of certificates so deposited nor upon mere loans of stock or the return thereof: *Provided further*, That the tax shall not be imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased same, but such deliveries or transfers shall be accompanied by a certificate setting forth the facts, etc., etc."

Respectfully submitted.

J. W. B. MALONEY,
R. TRACY FALK,
L. B. WILSON,

Committee Representing the Consolidated Stock Exchange of New York.

A PLEDGE.

[The Wall Street Journal, Monday evening, Apr. 15, 1918.]

To sustain the ruling of the Attorney General's department on taxing short sales, the distinction between a loan and an actual sale must be obliterated.

A baker's dozen of cases were cited as to the "fungible" (fusible) nature of securities, which, like grain, need not be returned specifically by the pledgee so long as he delivers out of the whole outstanding issue of the particular stock or bonds the amount in nominal value called for. Banking and brokerage usage in this respect have been upheld by the courts for over 50 years. The especial use to which the pledged security may be put has not been singled out by the courts, nor is it specified in the law of 1917 or any other law.

It was for this reason, and in accord with the authorities relied on by the department, that "a deposit of stock certificates as collateral" was expressly excepted from the 1917 law, and not embraced within any prior law, Federal or State. Therefore, to rely on these cases for the eagerly sought conclusion was to give them an interpretation making the exception of loan pledges from the law wholly meaningless and absurd.

As claimed by the department, a lender of stock for delivery by the borrower under contract of sale to a third party is not under contractual relation, or "privity," with them in the transaction. His contract is strictly one of loan, and of loan with the borrower only.

There is no just or essential distinction between a loan of money with "a deposit of stock certificates as collateral" and a loan of stock and a deposit of money as collateral for its return. This is not, as the opinion misconceives, the statement of a reverse result but a reverse statement in words of the same result. In each case one party wants the use of money and the other the use of stock. In each case one owes stock and the other owes money.

If the gratuitous distinction is warranted, it makes the principle of "mutuum," or loan exchange, identical with sale. To clear the grain of several owners from one elevator, for convenience, into the vessel of a purchaser who has not bought from any of them would be a sale. To justify the banker's use of current deposits, the fiction of sale would be indulged. So far afield, it is no wonder the opinion in fact cites a case of bank deposits as an illustration of its theory of sale fiction.

Senator THOMAS. The committee will take a recess until 3 o'clock, and then meet at the rooms of the Finance Committee in the Capitol building.

Senator PENROSE. I would suggest in the presence of the witnesses that that meeting is primarily to hear some theatrical people.

Senator THOMAS. We take a recess until that time in order to accommodate some theatrical people who are here from New York and want to get back.

Senator PENROSE. The others will get a fuller hearing if they will wait until to-morrow.

Mr. CALLBREATH. May I add that the mining people indorse fully the wording of the declaration clause of the present House bill.

Senator THOMAS. Certainly.

Mr. CALLBREATH. I would like to have that appear in the record.

(Whereupon, at 12.15 o'clock p. m., a recess was taken until 3 o'clock p. m.)

AFTER RECESS.

The committee re-assembled at 3 o'clock p. m. pursuant to taking of recess.

The CHAIRMAN. The committee will be in order. We will now hear Mr. Ligon Johnson. Will you proceed, Mr. Johnson?

STATEMENT OF LIGON JOHNSON, ESQ., GENERAL COUNSEL, REPRESENTING THE UNITED THEATRICAL MANAGERS' PROTECTIVE ASSOCIATION.

Mr. JOHNSON. Mr. Chairman, I represent the United Theatrical Managers' Protective Association. This association embraces every theater of any importance in the United States, covering the country from Maine to California, from the Great Lakes to the Gulf, and also includes all producing managers whose attraction play in these houses.

As a matter of fact, Mr. Chairman, and gentlemen, we have representatives here with us from each of the important theatrical and amusement enterprises in America; Mr. Marc Klaw, of Klaw & Erlanger, Mr. Lee Shubert of the Shubert interests, Mr. E. F. Albee, of the vaudeville interests, Mr. Savage, representing the producing managers generally; Mr. Winthrop Ames, of the overseas work, and others, and not only have we a representative of every other theatrical interest but also every branch of organized labor employed in theatrical enterprises, including stage hands, musicians, general employees in theaters, theatrical shop workers, and so on. We know that your time is limited and we do not expect you gentlemen to hear from all of them.

The CHAIRMAN. You understand that you have a right to submit briefs.

Mr. JOHNSON. Yes.

The CHAIRMAN. Will you divide up the time among these gentlemen?

Mr. JOHNSON. I will ask the committee first to hear from Mr. Marc Klaw, president of the Managers' Association.

The CHAIRMAN. Will you please state to the stenographer your name and address?

STATEMENT OF MR. MARC KLAW.

Mr. KLAW. Marc Klaw: New York City. I am not going to make a set speech to you. I saw what you are up against this morning, and I am going to be as brief as I can.

It is rather unusual for a theatrical delegation of any kind to ask anything. Our whole training in times of stress and trouble has been to give. I think you gentlemen, if you would look over the minutes of the hearing of a year ago, would probably find that there was no effort made by the theatrical people to lessen any tax, and there was no protest entered at that time, because we felt that the burden was here, and it was our burden and our duty to stand it as far as we could.

Senator THOMAS. Do you mean by that, that you had no delegation here asking for reduction of the tax?

Mr. KLAW. Yes, sir; I was here, but I made no request for a lessening of the tax.

Senator THOMAS. I have a very lively recollection that there was a request made of that kind.

Mr. KLAW. Yes, sir; I understand the motion picture men were here at one time and requested to be exempted; but we made no such request. At the time I was here the only thing I asked of Senator

Simmons was to have it clearly defined as to how the tax was to be collected, because I saw a great deal of trouble ahead at that time; and I think I suggested that a stamp tax would have been the easiest way to get the money, and the most economical of collection.

But when you come to doubling the tax, gentlemen, we are all very apprehensive after what happened last year in the first eight weeks, that you will legislate at least a certain proportion of the smaller managers out of existence. The public showed then that it did not like to pay ten per cent. It is all very well to say that they will pay any price for a good thing in New York, but New York is not the nation, and we found in going throughout the country that there was a great deal of objection to it. However, we got the public finally, after eight weeks—which, mind you, is twenty-five per cent of a theatrical season—where they paid it. But the business of the theaters suffered just about in proportion to that tax.

When the season was over we felt that we had given one performance out of ten to the Government.

The CHAIRMAN. Can you furnish the committee with any statistics showing the extent of the falling off of the patronage of your establishments?

Mr. KLAU. The theatrical concerns of the country?

The CHAIRMAN. Yes.

Mr. KLAU. I think I could; yes, sir.

The CHAIRMAN. We would be glad to have that.

Mr. KLAU. All right, sir; I will send that on.

Senator PENROSE. Roughly speaking, what percentage was it, do you think?

Mr. KLAU. I understand it was about 10 per cent. I understand that the New York Hippodrome looked into it and found out that it was just about that. My idea was that the average man had just about so much for amusements, and that was about as far as he could go. This report shows that about fifty million dollars was collected last year, which would show that the per capita expenditure was about five dollars.

The CHAIRMAN. Do you not think that in a great many sections of the country, especially where these war industries are located, the average man has a good deal more to spend for amusements now than he ever had before?

Mr. KLAU. We have not found it so. We have found that the theater has been hit in many ways. I am glad you opened that subject. In the first place, in England and France the theater has been helped. There are constantly a great many men at home on furlough. I understand that in London alone the home rest and furlough men average about seventy-five thousand all the time, and the theaters are full with that kind of patronage. We do not have that. Our men, unfortunately, go across the seas and they stay there until they come home—for good, we hope. The result of that is that we do not benefit by that kind of patronage at all.

In addition to that, I want you gentlemen to keep in mind the self-imposed tax that the theater has put upon itself in many ways. I happened to be interested in an entertainment that went out this spring that handed over to the Red Cross over \$700,000 as a result of its performances. That was the production of "Out there," which you may have seen here in Washington.

I was at a dinner last night of 25 managers called together by George M. Cohan and Mr. Ames, who is present here, who has charge of the overseas entertainment. Gen. Pershing has intimated that those boys there need more entertainment. There is no provision for it, and no appropriation, and I hardly think there will be any. The theatrical men night before last at that dinner—and there were not many men who are well-to-do there—pledged themselves somehow to raise the money necessary to send the additional units that are needed over there, and each individual got on his feet and pledged himself to send at least one unit, which means from four to six artists, to go over there and entertain those boys back of the fighting lines and in their rest places. Now, that is taking it directly out of our own pockets, besides disrupting many theatrical organizations, because we also pledged ourselves to stand in the way of no artist who wanted to go over there, but we would release them from their contracts; we would go further than that and extend the time when they returned.

In addition to this we are constantly giving these free entertainments. We are giving these entertainments in the camps; because you know, while there was an appropriation to build the theaters, there was no appropriation made to furnish entertainments. I was at the head of the military entertainment service at the time that was inaugurated. I do not want to become personal, but I am the inventor of the smileage book, and I do not mind telling you that when that was started, I advanced the money for the first one hundred thousand of those out of my own pocket, to have them printed.

The profession is willing to go just as far as you will permit it; but do not make it impossible for us to do the big things and the fine things we would like to do. We feel that for the first time in the history of this country the theatrical profession has had a national recognition. Strange as it may seem to you, this is the last country of the civilized countries that has given it that recognition. It has been recognized as an institution in foreign countries for many years. In England its members have been knighted, and honored in many ways. Until quite recently the theater has been tolerated in this country rather than encouraged. It has found its opportunity now, and I have never seen in any branch of industry or any profession anything like the willingness to take hold. We send men in all directions. Every time we send a man to a camp we set up an opposition to ourselves. If we send a company to Camp Gordon, which is near Atlanta, and give a performance for 25 cents, you know the big percentage of people are not going to see that show at Atlanta at \$1 or a \$1.50.

Senator SMOOT. May I ask you a question there?

Mr. KLAU. Yes, sir.

Senator SMOOT. Is there any way of differentiating the class of entertainments you speak of now and the class of entertainments that does no public entertaining, and that is in business just for the amount of money that can be made out of it?

Mr. KLAU. It is very difficult, because I believe nearly every branch of amusement has been contributing; but none of them has had the opportunity to do or has done as much of it as we have in what we call the spoken drama. We have got to do it. The spoken drama, which after all you must preserve, is the reservoir of all

these dramas. There would be no motion pictures without the spoken play, and yet we have become the by-product—or rather, say, the by-product have eaten us up. They are making more money than the original manufacturers. We are having a pretty hard time to get along.

You never hear of a theatrical company or theater having a strike. You have heard Mr. Johnson say that we are backed up by the musicians and the theatrical mechanics. We have raised the pay of these men this year as fast as we can and as high as we could, but we can not pass that up to the public. We are one class that can not make the public pay it. The tendency of the theater has been on the contrary in past years to lower prices.

Your bill is so framed that if we wanted to say tomorrow, "We want to include the war tax in the admission and charge \$2.25," it can not be done, because the war tax then would automatically become a part of the admission and the tax would be charged upon the two dollars and a quarter, and it would be twenty-two and a half cents instead of 20 cents. I had that up with Secretary McAdoo when the tax was proposed. The tax must be paid on the increased rates. I understand that it was framed in that way because you have no other safe way of collecting it. I have always felt that a flat tax would have yielded more revenue. If we had a graduated tax as we go up the line, with a maximum of, say, 25 cents, we could say to the public, "Here is a \$2 ticket," and we could pay the tax ourselves, and so long as the Government got 25 cents on every ticket of \$2 and over I believe that we would sell more tickets and you would get more revenue.

Senator THOMAS. Is it a fact that some theaters have not only added the war tax to their prices of admission, but have increased those prices also?

Mr. KLAW. I do not know of any theaters, in what I call the legitimate line, that have done so. I believe some of the motion picture theaters have done so.

Senator THOMAS. Is Keith's a legitimate line theater?

Mr. KLAW. I would call that vaudeville.

Senator THOMAS. I am told that they have done it in this town and in other places; that they have taken advantage of the tax and added not only the tax but added to the price of the ticket.

Mr. KLAW. Keith's is a very much cheaper house than the legitimate.

Senator THOMAS. It was.

Mr. KLAW. I do not know what their prices are. But do not forget when you speak of Washington and New York—I do not know that I need go any further than that—those two cities are exceptional, just now, because of the immense population that is drawn to them. You find the result in your hotels and everywhere else.

Senator THOMAS. Yes. I was told by one man about being charged an increased price at that theater.

Mr. KLAW. I know we have the tendency with us to lower prices. In New York City the prices go up, but in New York we are cursed with the middleman, the speculator, which makes it impossible to get the price down; and I wish to heavens you had made it, in framing your bill, so that any man that buys a ticket outside of a ticket office would be taxed 100 per cent.

Senator McCUMBER. I think we can accommodate you.

Mr. KLAU. I wish you would. I have gone before the Board of Aldermen, and have failed in it. I went before the Legislature in Albany with a bill that the Bar Association of New York said would hold water and was constitutional, and I was met there by a great array of counsel representing hotel owners, who knew that if that thing was done, these news stands in the hotels could not charge these fancy rentals; because they do not make \$10,000 a year selling newspapers. We are helpless about that.

Mr. JOHNSON. There was an amendment like that, and it was stricken out in conference of the two houses.

Senator THOMAS. We can not take into consideration, in a bill like this, those peculiar things that differentiate Washington from New York, and we have to legislate generally. A friend of mine tells me that he went to Keith's a while ago, and he paid \$3.30 for two tickets—that is, a dollar and half each and 30 cents war tax. Before we passed this bill the admission was about 50 cents, was it not?

Mr. KLAU. That may be true; but I will venture to say that the expenses of Keith's and any other theater have gone up 70 per cent in the last three years.

Senator THOMAS. They have gone up some, but not enough to justify such public robbery as that.

Mr. KLAU. I am not willing to admit that it is robbery, although we do not do it. My personal experience is that our expenses have nearly doubled in the last three or four years. It began just before war was declared, and the tendency all the way through was to keep the prices where they were. You may say that you can get \$7 for a good show, and I will admit it; but you will not get it for enough tickets to yield the additional revenue that you gentlemen are after and that we all hope that you will get. I remember Joe Jefferson said to me some years ago that he always liked to go through the country in times of panic and in bad times, because then everybody concentrated on a few shows. Concentrating on a few shows will not answer your purpose. If you want to collect the additional revenue which you need, you need more admissions instead of less. If you drive the people away from \$2 theaters and make them depend entirely upon the cheaper priced theaters, you will not get as much money.

Senator PENROSE. Do you think that a possible outcome of this increased price might be a less revenue?

Mr. KLAU. Yes, sir, it will result in less revenue, because I am confident that there will be less companies. They can not exist. Gentlemen, I would not make such a statement as that in a company like this if I did not honestly believe what I was saying, because after all, you are only asking us to be the collectors for you, to be the collectors from the public, and if we believed we could get it for you, we would not hesitate for a moment to try to do so.

You know in Canada after three years of war they have no such tax as this of ours, and in France some theaters are subsidized. In Germany nearly all of them are subsidized, because they felt that they wanted to keep the theaters open. I feel that the theater has become an arm of this Government in the last eighteen months. We set aside everything else and we open our doors for thrift stamps,

for everything they ask of us. That has lessened patronage for us. I have heard a man say, "I do not want to go to the theater any more, because, in addition to sitting there, I am always boned to buy something." We are willing to "bone" them for you. We feel that we should do it, and that we are in this hour public institutions; but we are giving away a great deal. The income-tax reports are accessible to you, and you can see what the theater managers have made. There may be a few of them that have made a lot of money, but not many of them, and we are talking now for the rank and file. I feel that we are doing, and are going to do, everything we possibly can.

Senator THOMAS. Is yours an incorporated company?

Mr. KLAU. No, sir; we are a partnership. I understand that the theaters last year raised over one hundred million dollars. I know that the Stage Woman's War Relief raised over fifty. I know that your theater here in Washington, Keith's Theater, sold \$4,500,000 of Liberty bonds; and I believe that all the way through we are a source of patriotic propaganda, and I think it would be a tragedy to close any of them up. I believe honestly that some of them will have to go by the board. I had a man tell me that in the west they never did get over that 10 per cent tax all the season.

I do not know of anything more I can say. I am talking to a sympathetic audience here, because most of you know what the theater has tried to do.

The CHAIRMAN. Am I to understand that you suggest the tax shall not be increased at all or that it shall not be increased as much as in the House bill?

Mr. KLAU. I do not think that the tax should be increased at all. I think if you tried for a few months the present tax you would find that your revenue would increase. You may say, "We have a gentleman here representing the Metropolitan Opera House. Those people can stand it." But the trouble is that even the Metropolitan Opera House can not stand it. Mr. Ziegler wants to tell you they could not exist if it were not for the balcony and gallery patronage. That is, the so-called high-class people do not in the long run support the theater. The best evidence that you can get of that is to go into any theater in New York City that has a tremendous success, and I would make a wager that after six weeks the boxes are empty. They last for a very short while; and you know it is in the theater like in everything else, the middle class support it. They will shy at paying 40 cents on a \$2 ticket, and they will simply say "I can go to a picture show for 40 cents and take my wife." We can not do things that way.

The CHAIRMAN. You do not mean what you have said to apply to moving picture shows?

Mr. KLAU. No; I am not speaking for them now, because I understand they had a hearing before. You add 20 per cent on a 25-cent ticket and it is 5 cents. It is very different when it comes to a \$2 ticket. This \$2 theater, you may say, is a luxury. The administration and others have told us that it is an essential in time of war. We believe it is absolutely essential. It is the only luxury that the poor man has. If it is a luxury, he can even once in a while pay \$2 and see what he calls a high-class entertainment.

The CHAIRMAN. To what extent is the Government encouraging these entertainments behind the front in Europe?

Mr. Klaw. I do not believe that the Government has done anything except to give it a formal recognition. I believe the Y. M. C. A. has some money for that purpose.

The CHAIRMAN. I do not mean by pecuniary contributions, but is the Government pursuing a policy encouraging it?

Mr. Klaw. Mr. Ames can tell you more about that. He is right here.

Senator THOMAS. While you are on the floor let me ask you what percentage, approximately, of theater tickets are sold at the news stands in the hotels and by scalpers.

Mr. Klaw. Where? Because I believe they are only sold—

Senator THOMAS. I mean in New York:

Mr. Klaw. In New York City?

Senator THOMAS. Yes.

Mr. Klaw. I really could not tell you, but it is entirely a question of the play if you have a very big success.

Senator THOMAS. I supposed that being in the business you would have some idea about it.

Mr. Klaw. I would not, and I will tell you why. This hotel question is a very peculiar one. When we first went into the theaters of New York, when I first came there, we used to give to each hotel a certain number of tickets. It usually amounted to about 80 in all, sometimes as high as 90, which did not seem to be very much.

Senator THOMAS. You mean you left them there for sale?

Mr. Klaw. Yes, with 15 or 20 hotels. There soon came a time when these hotels would put men in the line to do what we call "dig" for them; they would get in line and buy all the best seats whenever you had a big success. That led to the most natural thing in the world, corruption in the box offices, where the treasurers—we call the ticket sellers treasurers—some of them would get in with these fellows and they would be bribed and they would sell them the best tickets, and sometimes perhaps take them back if they were not sold. I do not know that that occurred often, but we heard that it did and we found one example of that and discharged the man. A great many of the theaters declined, then, to give them any tickets. The hotel agencies then would go to a theater, just as they do in London, and say, "We would like to make what is called a buy-out; we will take so many seats a night for four or six weeks and pay you for them and pay a premium besides." Some of the theaters made a deal with them like that. I think, myself, they were justified when you consider the uncertainties in New York on account of storms and blizzards and other things. I believe it was a bad thing for the theater, however, because the public never would believe that we sold the tickets at only a slight increase, or that we did not stand in with those who sold the tickets at exorbitant prices.

We then made an agreement with the hotels not to charge the public more than 50 cents. That is, a \$2 ticket would be sold for \$2.50. They signed an agreement to that effect, but it was the easiest thing in the world to avoid it, because all they would do would be to have some outside agency, and give him the tickets to sell at \$2.50, and he would sell them at what he pleased. All the hotels to-day are pledged to sell those tickets for \$2.50. But if you go to some hotel to-day that does not want to be honest with you, it will tell you,

"I have not any tickets, but perhaps I can get them for you from some outside agency;" and that is the way it is worked. I do not think there is a theater in New York city that would not like to keep that thing down to \$2.50, because I think the theaters would make a good deal more money; but the business has almost slipped out of their hands when you have a success in a city like New York.

Senator THOMAS. Putting aside for the moment consideration of the hotels, there is a very large percentage of tickets that are also put out by scalpers?

Mr. Klaw. There are no ticket scalpers in New York any more. They have been legislated out of existence.

Senator McCUMBER. I want to just ask one question for information. What per cent of the expense of operating the theater is paid out to actors and performers, etc?

Mr. Klaw. It is difficult to answer that question, because I think it is founded on perhaps a lack of knowledge, if you will pardon me, on your part. The theater and the performer are two separate entities entirely. A theater is leased by a manager—that is, what we call a theater manager, a local manager, and the production is furnished by a producing manager. It sometimes happens that the two are identical, as in the case of Mr. Belasco and his theater. He rarely plays anything in there except his own companies. I should say that the salaries of actors in a dramatic company would be 70 per cent of the entire running expense. That is, when I say "actors," I mean to include in that the mechanical facilities necessary to give a proper performance. Then, as against that, the theater has its expenses, with its orchestra and heat and light, etc. That is a separate thing. We generally play on what we call a percentage basis. If I had an entertainment and you were running the theater, I would come to you and make the best terms I could for my production in your theater, giving you a certain percentage of the gross receipts, out of which you, as manager, would pay the expenses, lighting and heating, and orchestra, etc., and I, out of my percentage, would pay my royalties on the play and my other expenses.

I would like Mr. Ames to say something to you, Senators.

The CHAIRMAN. Very well; he may proceed.

STATEMENT OF MR. WINTHROP AMES, OF NEW YORK.

Mr. AMES. In February last Gen. Pershing asked to have sent over to France a representative actor and a representative manager to see what could be done with reference to supplying entertainment to the boys in France, and Mr. E. H. Southern and I went over and went on a tour through France to see what could be done. We came back and made our report to Gen. Pershing, who approved our scheme and said go ahead with it, but to go ahead with it through the Y. M. C. A., because they have the only available auditoriums in which entertainments can be given.

We came back and reported to the Y. M. C. A., who agreed to pay two-thirds of the expenses, and as Mr. Klaw told you that the managers agreed to furnish one-third of all these expenses, and we are endeavoring now to send weekly at least 50 performers, of the best class, to France, and maintain at all times over there at least two hundred performers, and they will need more than that, I think.

That is, in a nut-shell, the whole thing. The Fosdick Commission has approved it. But it is a purely charitable undertaking, on the part of the theaters and the Y. M. C. A.

The CHAIRMAN. You do conduct performances for the boys behind the lines?

Mr. AMES. In the case of the individual performer, they can go almost up to the gas line.

The CHAIRMAN. Do any of our allies over there encourage like amusements for their soldiers?

Mr. AMES. Indeed they do, very much. I think the most interesting thing is the Canadian experiment. For several years of the war they have made what they call an amusement factory, in which they have a hut more or less like the hut they have overseas, with a camouflaged audience, and they will take an artillery gunner if he can whistle through his teeth, for instance, and put him in there and train him so that he can entertain the soldiers. He is still in the service, he has got to get up at reveille, he is a soldier just the same, but he is taken out as an entertainer to help maintain the morale; and the person in charge of that told me that in the present stage of development of the Canadian Army, instruction in fighting is put at 50 per cent and morale at 50 per cent, according to his idea after three years of war. Is that what you wanted to know, sir?

The CHAIRMAN. Yes, sir. Does any other gentleman desire to be heard?

Mr. JOHNSON. It may interest you gentlemen to know what the present taxes in Canada, after several years of war, are in comparison to our taxes here. I have here a compilation made just a few days ago.

The CHAIRMAN. What are you speaking about, the present tax or—

Mr. JOHNSON. I am just giving you a comparison of the present taxes in Canada and those of the United States.

The CHAIRMAN. Are you comparing that tax with the existing tax here or with the proposed tax?

Mr. JOHNSON. With either, because it follows that the relative percentages under comparison would be doubled in the case of the proposed new tax.

In Ontario the tax on admission from 1 to 20 cents is 1 cent, from 20 to 50 is 2 cents, from 50 cents to \$1 is 5 cents, and anything over \$1 is 10 cents, the maximum tax in Ontario being 10 cents.

In Quebec the taxes are from 1 to 25 cents, 2 cents; from 35 to 74 cents, 3 cents; from 75 cents to \$1.49 cents, 5 cents; and anything over \$1.50, 10 cents.

The CHAIRMAN. Have you the taxes imposed in Great Britain and France?

Mr. JOHNSON. Not of any laws enacted recently, sir. They were considerably less than our present taxes under the old régime. I do not know whether or not any new revenue bill has been introduced in Great Britain, and for that reason I am not able to inform the committee as to the present rate. The United States taxes were much higher in the beginning than those of England.

At one time France proposed to levy an excessive amusement tax, and this resulted in closing the French theaters. That tax was

subsequently revoked when it was found that the theaters could not live under it.

I wanted to say one other thing. The theater alone of all enterprises in war times can not pass its increased costs onto the public. Compare, for example, a theater with a shoe manufacturer. The shoe manufacturer pays more for his leather and more for his labor and more for his cost of distribution. He adds that onto the price of his shoes. The \$5 shoe of two or three years ago is now about \$9 or \$10. The theater manager pays more for his canvas, more for his paints, and more for his costumes. He has been forced to increase his overhead cost and the scale of wages for his labor. He pays more to his actors. Yet he is unable to pass one penny of all this along to the public. He can not increase his prices. So that, regardless of taxes, the theater is now bearing a much heavier burden than it did before the war.

Senator THOMAS. Does he not increase his prices?

Mr. JOHNSON. No; he does not. You may find one instance in New York and one in Washington; but we are speaking now of the country at large. It is absolutely impossible to increase the theatrical prices, and the present tendency is, as Mr. Klaw said, to lower them throughout the country. You see, the public has gotten the idea of saving, investing in war-savings stamps and in partial-payment bonds, so that all of the tendency of the times is toward economy, and any increase, even the 10 per cent tax increase, has a very material effect upon the public at large. I have heard people say of the 10 per cent increase, "We will not pay it," and time after time we have seen people turn away and walk out just because of this 10 per cent increase charge, and that after they had actually gone to the theater to buy their tickets. We firmly believe that increased tax will actually reduce the amount of revenue to the Government, because the tendency is to go to the cheap-priced amusements. The salaried man furnishes the main element of the theater's audience. The average salaried man's income has not been increased, while the purchasing power of the money he gets has been woefully diminished. He must economize.

Now, the theaters furnish the real audience that the Government desires to reach on its propaganda campaign. These audiences are composed of the people to whom you sell your bonds and your thrift stamps.

These are the people that the Food Administration wants to reach, the Fuel Administration wants to reach, and the various other agencies of the Government want to reach. There is not a theater manager throughout the country whose desk is not piled with slides from some agency of the Government. We receive and promulgate all the Government propaganda, and while we all know the value of the newspapers in bringing before the people the things that the Government desires the people to know we believe the theaters are hardly second to the papers in this work. A man with his newspaper reads or not as he feels inclined the articles which have been put there through the intervention of some Government agency. It is quite the contrary in the theater. To begin with, in the theater you have a ready-made audience; you have an audience which is obliged to hear your four-minute speakers; you have an audience which has to read the things that your slides show. If the theater

managers gave the empty theaters to the Government, and instead of spreading the Governmental propaganda at regular performances—just gave the empty theaters outright—you could never get an audience in them merely to look at slides or listen to four-minute speakers. So that in all theaters work for the Government propaganda not only goes a great way but is very materially aided by the opportunity of reaching the type of citizen that the Government most wants to reach, and we believe that by decreasing the audiences in the theaters you will not only have a resultant loss of income by the Government, but you will lose also the opportunity of propaganda that I think the Government so much wants at this time.

Mr. Klaw. Senator Simmons, I just want to say one thing and put one more thought in the minds of you gentlemen before we leave you. I said that the theater is hit in many ways, and it is. The new draft is going to hit the theater very severely. The average man in the theater is wedded to an actress, and he can not claim exemption on the ground of dependency and he will have to go; and we need encouragement now about as much as any profession or industry I know of.

The CHAIRMAN. Is there anybody else to be heard.

Mr. JOHNSON. We will ask the committee to hear Mr. Robbins, of Keith's theaters.

The CHAIRMAN. We will be glad to hear from Mr. Robbins.

STATEMENT OF MR. R. S. ROBBINS.

Mr. ROBBINS. I just want to say, Mr. Chairman, since a member of the committee has spoken of it, that the prices at Keith's Theater for the first 12 rows are \$1.50, and for the remaining rows \$1. Last year the first six rows were \$1.50. Two weeks ago, the week of August 27, we moved the price back six rows.

On the mezzanine floor, or the first balcony, where last year the seats were 50 cents, and 55 cents including the war tax, they are now 83 cents, or 75 cents plus 8 cents war tax. That is the only increase in prices at Keith's Theater.

Now, anyone who is a regular habitue of Keith's generally assumes that he gets his money's worth. Senator Smooth, I think, is a regular attendant; I see him there frequently.

Senator McCUMBER. President Wilson seems to be there pretty often.

Mr. ROBBINS. Yes, sir; and they come regularly. And I do not think if they were overcharged they would be so consistent in their patronage.

I might say that at Keith's local Washington theater we hold the record for sales of liberty bonds. In four weeks in that house we sold \$4,271,000 worth of bonds.

In the war-savings drive I was made chairman of the committee on activities in the theaters of the city of Washington, and I sold \$100,000 worth of stamps in 12 days in Keith's Theater, and through my direction in the other theaters another \$100,000 worth of stamps.

In the Red Cross drive, in a week I collected within \$200 of \$25,000 for the Red Cross.

In addition to that, as a matter of fact, I would like to say here that propaganda in all theaters began in this local Keith's Theater.

here. I started it myself with a babies' campaign, or a campaign for the benefit of babies in the summer, four years ago.

I would like to say, too, that in the last few weeks we have increased the wages of our stage employees 40 per cent.

Senator THOMAS. Do you not make an extra charge for Saturday night performances?

Mr. ROBBINS. No, sir.

Senator THOMAS. Have you never done that?

Mr. ROBBINS. The only extra charge on Saturday nights, last year the first five rows in the mezzanine floor were 75 cents and on other nights of the week 50 cents.

Senator THOMAS. What were your prewar charges—your charges for tickets prior to our entry into the war?

Mr. ROBBINS. That was three years ago.

Senator THOMAS. No; I do not mean at the beginning of the war, but at our entry into the war—in April of last year.

Mr. ROBBINS. Exactly the same as they are, except we have this year moved the \$1.50 rows back six rows and made the first five rows upstairs 75 cents.

Senator SMITH of Georgia. You did not make any increase in the fall of 1917?

Mr. ROBBINS. In August, 1917—that was last year, in August—we made the first six rows in the orchestra \$1.50 where they had been \$1.

Senator THOMAS. Are you going to keep moving that price back as the war continues?

Mr. ROBBINS. Well, that depends.

Senator TOWNSEND. How long ago was it that you raised the salaries of your stage employees?

Mr. ROBBINS. That was August 1.

Senator TOWNSEND. Of this year?

Mr. ROBBINS. Yes, sir.

Senator TOWNSEND. You had increased your prices for admission before you raised any salaries?

Mr. ROBBINS. On August 26 our prices were increased.

Senator TOWNSEND. Why was it necessary for you, owning that theater, to increase your prices of admission if you had not increased the wages of your employees? Why did you increase your prices?

Mr. ROBBINS. Because the demand for the tickets warranted it.

Senator THOMAS. That is, your audiences increased; the number of your audiences increased?

Senator TOWNSEND. That was August 1 of this year, as I understand, and you raised your prices of admission a year ago last August?

Mr. ROBBINS. Yes; that is true: \$1.50 for the first six rows.

Senator THOMAS. How many performances did you give before the war here in Washington?

Mr. ROBBINS. We gave two performances a day.

Senator THOMAS. Including Sundays?

Mr. ROBBINS. Yes.

Senator THOMAS. Just as you do now?

Mr. ROBBINS. Yes.

Senator THOMAS. When did you begin giving 2 performances a day or 14 performances a week?

Mr. ROBBINS. That has always been the policy of the theater.

Senator THOMAS. I know; but actually; when did you actually begin that here?

Mr. ROBBINS. Five years ago.

Senator THOMAS. Five years ago?

Mr. ROBBINS. Yes. Now, of course, Mr. Klaw has already drawn your attention to the fact that the expenses of the theater have increased steadily, too, in the last five years. Every year we pay a little more to everybody.

Senator THOMAS. Everything has gone up except Senators' salaries.

Mr. JOHNSON. I would like to have you hear for just a moment from Mr. Savage.

The CHAIRMAN. All right, you may begin, Mr. Savage.

STATEMENT OF MR. HENRY W. SAVAGE, OF NEW YORK.

Mr. SAVAGE. I appear, gentlemen, as representing the type of manager known as the producing manager, who has no theater or headquarters of his own, who engages a theater, gets together his own show, goes to New York and stays there perhaps a few weeks, and goes, then, on tour. Working in that fashion we have to keep very closely in touch with the country throughout, and it took us at least three months last year to get the public habituated to the payment of the 10 cents extra tax. Since then I find in the smaller cities—not in the larger centers like New York and Boston, but in the Romes and Uticas and the smaller cities throughout the country—that it has affected the theater business greatly.

We have now, according to the newspapers, some 1,500,000 men of theater-going age in France. Those men used to go to the theaters, to take their sweethearts or wives or sisters. Perhaps one or two out of every three spent \$1 to \$2 a week in that way, which is not much, that are not doing that now. That is over \$1,000,000 a week which has been taken out of our local market in the last few months, and it is increasing. This is being shown by the number of women who are paying their own way. I have the practical experience, because in this matter of traveling attractions I am used to having to watch these things closely. In more than half the cases under the present tax increase it was the woman who would decline to pay; it was the woman who would take the man by the sleeve and say, "Come away"—who objected to paying that extra 10 cents tax.

Mr. Johnson has spoken to you of the shoe business, contrasting it with the theatrical business. There is this difference between the man who manufactures light opera, like I do, and the man who manufactures shoes: The man who makes those shoes can sell those shoes for some time after they have been manufactured. I can not do that. If a ticket is not sold for a performance then that place is vacant; that is a positive loss. We can not wait until the sixth performance; we can not wait for my lady to make up her mind to come back again. In other words, gentlemen, it seems to us as a purely business proposition that when our business is decreasing and is going to decrease more, it is a mighty poor time to increase prices, on a falling market.

Now, turning to the enormous by-product which the theater has given in and through the presentation of information to our audi-

ences, that hurts us, psychologically, gentlemen. It hurts more than the amount that they take out, for this reason: A member of the audience is interested in a production and his interest is keyed up at the end of the second act, and then comes an eight-minute speech, telling of the horrors of war. His mind is taken away from the play and we can not get him back, and if most of the audience feels the same the new piece is likely to be a failure. That is actually happening. We have given our intermissions to the Government and are going to do it. But so far as I can make out, thinking over it, with my knowledge of it, I think the proposed tax would make a difference of 30 per cent in the business.

Senator THOMAS. Let me ask you whether this was submitted for the consideration of the Committee on Ways and Means of the House?

Mr. SAVAGE. No, sir.

Senator THOMAS. You gentlemen did not appear there?

Mr. SAVAGE. No, sir.

Mr. KLAW. It has never been presented to anybody except you, here.

Senator SMOOT. What is the price of the lowest-priced ticket of admission with the companies you refer to?

Mr. SAVAGE. That is according to the house. Usually it is 35 cents for the gallery and \$1.50 for the orchestra. In the cities we charge \$2.

I was talking to a man yesterday morning who used to be my Vienna representative on the other side, and he tells me that there, and also in Berlin, far from imposing any tax, the subsidies were being increased. There are 75 houses in the German Empire that are subsidized. Many theaters were closed, and they were so convinced of the necessity of maintaining the theaters that they said, "The theaters must remain open; the morale of the people must be maintained. Go ahead, and we will pay the bills."

Senator TOWNSEND. Do you show any of this war work in connection with your performances?

Mr. SAVAGE. We show it between the acts. This is furnished by the departments of information. It is particularly true throughout the West. They would not give a performance without war propaganda any more than we would without playing the Star-Spangled Banner.

Senator TOWNSEND. Do you maintain that those entertainments are a detriment to you?

Mr. SAVAGE. No, sir; and it is not the four-minute man that hurts us, but it is sometimes the speaker who is in love with his own voice, like one who on the night of a new production told me that he would take 4 minutes and spoke 14 minutes.

Senator TOWNSEND. What I speak of is a performance of war pictures and propaganda, so advertised.

Mr. SAVAGE. It is not so with us. If there is anything of that kind it is between the acts.

Senator TOWNSEND. But do not those performances help you by drawing more people?

Mr. SAVAGE. No, sir; they deter them.

Senator TOWNSEND. It is my experience, from what I have seen, that where those were advertised on the bill the theaters have been crowded.

Mr. SAVAGE. Our theaters, Senator, are what are known as the legitimate shows; that is, the two dollar attractions, not the moving picture houses.

Senator TOWNSEND. I asked you if you had used those things in connection with your performances?

Mr. SAVAGE. I understood you to mean in connection with the war work, the propaganda.

Senator TOWNSEND. In connection with your play?

Mr. SAVAGE. They are shown between the acts of the play.

Senator TOWNSEND. And it is advertised that they will be shown?

Mr. SAVAGE. Not usually, I believe. How about that?

Mr. JOHNSON. The slides that we show are of the Food Administration and the Fuel Administration, "Save the wheat," and "Save the meat," and "You are limited to two lumps of sugar." It is that character of slides. We do not show in our theaters at all the pictures that are taken abroad of the troops. Those are in the paid motion picture houses, and are a part of the paid entertainment. As a matter of fact, the Government is getting considerable revenue from that. Gen. Newton can tell you about it. He, as a western theater manager, can tell you better about that.

Mr. KLAU. Mr. Chairman, Gen. Newton is manager of a theater at Springfield, Mo., representative of that kind of theater to-day, in a city of about 50,000, which is a better average to judge by than New York.

The CHAIRMAN. Gentlemen, after this speaker has finished I think we will have heard enough.

Senator PENROSE. I want to ask one question of this last witness, about the Government and the moving picture houses. Do you pay the Government so far as the receipts of those houses are concerned?

Mr. JOHNSON. We have one film that is doing an enormous business that was exhibited in the Cohan Theater, I think, in New York. For that film a regular admission was charged, and a very large business was done, and on those pictures, of course, no tax whatever was exacted from the public.

Senator PENROSE. What is that picture you refer to?

Mr. KLAU. America's Answer. It was the second of the Creel series.

Senator PENROSE. Then the Creel Bureau is a profitable, money-making concern?

Mr. KLAU. That picture did a very good business.

Senator PENROSE. That is very cheering. They are nice people, and I have been only familiar with their expenditures.

The CHAIRMAN. Proceed. Gen. Emmett Newton will be heard now.

STATEMENT OF GEN. EMMETT NEWTON.

Gen. NEWTON. In towns of 50,000, towns that we call the one and two night stand attractions, where we are only open a part of the time, we depend on road shows. Now, our theater is the only place for the people to gather in that town. If you have meetings of any kind they are held in our theater. I have given my theater 165

times since the war opened, free. My desk is packed with slides from the Food Department, from the Fuel Department, from all branches of the Government. If they call for stenographers they send us slides and that propaganda is thrown on our screen. We run our screen down during the performance, and if a four-minute speaker comes in we give him the right of way. He occupies not only 4 minutes, but sometimes 30 minutes or 40 minutes. We are glad to respond in any way, and we are called on at all times for the Red Cross and for all kinds of charities.

In towns of our size the theater is the only place where meetings can be held in the town. Now, if you put the extra tax on us we will really have to close our doors, because we have so few attractions, and with the patronage curtailed as it has been it will absolutely put the theaters of our sized town out of business.

The CHAIRMAN. Next gentleman to appear is Mr. Edward C. Crow.

STATEMENT OF MR. EDWARD C. CROW.

Mr. CROW. Mr. chairman and gentlemen, I know that you are anxious to get away; you have been here a long time. I just want to say that I represent a different class of amusements from any that have been mentioned, and I would like to have the privilege of filing a statement.

The CHAIRMAN. What class of amusement do you represent?

Mr. CROW. The outdoor park amusements.

The CHAIRMAN. You may do that.

Mr. CROW. I will just file a statement, and permit me to say that if the tax proposed is put upon our class of entertainment we will have to retire from business.

(Mr. Crow subsequently submitted a statement, which is here printed in the record in full, as follows:)

The old act, effective October 3, 1917, provided as follows:

"(a) a tax of 1 cent for each 10 cents or fraction thereof of the amount paid for admission to any place, including admission by season ticket or subscription, to be paid by the person paying for such admission: *Provided*, That the tax on admission of children under twelve years of age where an admission charge for such children is made shall in every case be 1 cent; * * *

This enactment, of course, covered admission to outdoor parks, the charge for which to most first class outdoor amusement parks is 10 cents.

There was attached to this section of the act, effective October 3, 1917, the following amendment, to wit:

"These taxes shall not be imposed in the case of a place the maximum charge for admission to which is 5 cents, or in the case of shows, rides, and other amusements (the maximum charge for admission to which is 10 cents) within outdoor general amusement parks, or in the case of admissions to such parks."

The amusement parks, as a rule, have a great many shows, rides, and other amusements within the general inclosure, and the charge for admission into the general inclosure does not include entrance into or rides upon these various amusements located within the general inclosure. As a rule, these shows, rides, and similar amusements within the park charge an admission of 5 cents or less and are largely patronized by children and ladies. In case of the St. Louis Park, ladies and children are admitted every day during the short season (which is four months, beginning in May and ending first of September) free of charge at the outer gate up to 6 o'clock p. m., and hundreds of thousands of free admission each summer are given in this way to mothers and their children.

Under existing law the tax upon the amount paid for admission to the park is 1 cent for each 10 cents or fraction thereof of the amount paid for such admission. The proposed new revenue bill increases this tax to 2 cents for

each 10 cents or fraction thereof of the amount paid for admission. Under existing law and under the new revenue bill, in the case of children under 12 years of age, the tax upon such admission will be 1 cent, regardless of the amount paid for admission.

As will be observed from the foregoing statement, under existing revenue law there is no tax levied upon admission to any place the maximum charge for admission to which is 5 cents, or in the case of shows, rides, and other amusements within outdoor general amusement parks, or in the case of admission to said park where the maximum charge for admission is 10 cents. The proposed revenue bill provides, in lieu of this provision, that in cases where the charge for admission is 7 cents or less the tax shall be 1 cent.

The proposed tax will decrease very largely the revenue tax received from outdoor amusement parks, if it does not, in fact, close most of them, for the reason that it is the tax upon the amusements of a class of people who can not meet the increased cost proposed in this revenue bill. The following is a copy of the proposed new section in the pending revenue act.

"(1) A tax of 2 cents for each 10 cents or fraction thereof of the amount paid for admission to any place on or after such date, including admission by season ticket or subscription, to be paid by the person paying for such admission: *Provided*, That in cases where the charge for admission is 7 cents or less, and in the case of children under twelve years of age where an admission charge for such children is made, the tax shall be 1 cent."

The old enactment of 1917 produced a very handsome revenue from parks for the four months' season which has just closed, and in the opinion of those best acquainted with this business the proposed act should be in the terms of the act of 1917, which would make it read as follows:

"(a) A tax of 1 cent for each 10 cents or fraction thereof of the amount paid for admission to any place, including admission by season ticket or subscription, to be paid by the person paying for such admission: *Provided*, That the tax on admission of children under twelve years of age where an admission charge for such children is made shall in every case be 1 cent; * * *."

"These taxes shall not be imposed in the case of a place the maximum charge for admission to which is 5 cents, or in the case of shows, rides, and other amusements (the maximum charge for admission to which is 10 cents) within outdoor general amusement parks, or in the case of admissions to such parks."

It would seem that there could be no justification for imposing a 2-cent tax on free admissions to any place of amusement.

The above taxes have no reference to theatrical performances which many of the larger parks have within the general inclosure and upon which theatrical tickets the usual levy under the revenue act for theatrical exhibition is made in collecting.

The CHAIRMAN. This ends the hearings for to-day. We will now adjourn until to-morrow.

(Thereupon, at 4.05 p. m., the committee adjourned to meet at 10.30 o'clock a. m., Thursday, September 12, 1918.)

TO PROVIDE REVENUE FOR WAR PURPOSES.

THURSDAY, SEPTEMBER 12, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10.30 o'clock a. m., in the committee room, Senate Office Building, Senator Boise Penrose presiding.

Present: Senators Smith, Thomas, Robinson, Jones, Gerry, Nugent, Penrose, Lodge, McCumber, Smoot, Dillingham, and Townsend.

The committee resumed the consideration of the bill (H. R. 12863) to provide revenue, and for other purposes.

Senator PENROSE. In the absence of the chairman, I will call the committee to order. The first gentleman on the list to be heard this morning is Dr. Lindsay, who wants to be heard on the inheritance tax. What is your present position?

INHERITANCE TAX.

STATEMENT OF DR. SAMUEL McC. LINDSAY, OF COLUMBIA UNIVERSITY.

Dr. LINDSAY. Professor in Columbia University, New York City. I need only a minute or two to state the matter to which I want to invite your attention, as I think it is already familiar to all the members of the committee, and I think has their sympathetic interest. It is the question of introducing in the proposed revenue act, under the deductions allowed in section 403, the proposal to exempt from the estate tax bequests and legacies for charitable, educational and religious purposes.

An exemption is already allowed for gifts and donations for such purposes from the income tax. That was put into the revenue bill last year, up to 15 per cent of the otherwise taxable income. Therefore the principle was recognized of exempting from taxation property already devoted to a public use. It would seem almost like a double tax to tax a gift for a public use.

It was not applied, however, to the estate tax, and the matter I want to call to the attention of the committee is that, from the point of view of the interests of the educational institutions in the country and of the philanthropic institutions, especially the hospitals, it is even more important, if you want to encourage that work, to exempt bequests and legacies from the estate tax than it is to exempt gifts and current contributions from the income tax, because these institutions rely very largely upon the accumulation and succession of

gifts, many of them in large amounts, that come from bequests and legacies.

I need not say very much, I think, further than to call attention to that point, because the need of this thing is so apparent, there is ample evidence of it, and I think that has been presented perhaps to the committee already in the form of letters from former President Taft, and President Lowell of Harvard University, President Butler of Columbia University, President Hibben of Princeton University, and practically all of the college presidents.

I would also like to call attention to the fact that a very great deal of evidence of the need of this thing has been presented lately to the Ways and Means Committee by the American Hospital Association's committee on war emergency, in view of the great work that has been put upon hospitals in cooperation with the Government, and their extreme financial need at present. Hospitals, perhaps more than any other class of institutions, are affected by any falling off in the small legacies that are usually part of a residual estate, and therefore meet the full burden of this tax.

The only question involved is whether you must necessarily consider the effect of a tax upon the general policy of the country, which has been to rely upon private benevolence to support the great institutions of education and of philanthropy. That has been our traditional policy from the beginning of this Government. Of course, if it is the intention of the Government to change that policy, and to go over to a policy that is more familiar to Europeans than it is to Americans, of Government subsidy and support of such institutions, that is another matter. In Germany the 21 leading universities are practically supported entirely by government contributions, that is, by taxation. In England and France and other European countries the amount of tax support that is given to universities and colleges and hospitals, and charitable institutions of all kinds, is enormously larger than anything we do in this country, or ever have done.

(Senator Simmons thereupon entered the room and took the chair.)

Senator THOMAS. You mean larger than anything we have done?

Dr. LINDSAY. Or anything we are doing now.

Senator THOMAS. I understand the Government has taken over 400 educational institutions, and is practically supporting them at the present time.

Dr. LINDSAY. The Government is planning this year to send a great many of the soldiers for training, the drafted men, to some 400 institutions. How much support that will be I do not think any of us know yet. It would affect, however, only a small number of the institutions.

Senator ROBINSON. My information is that there is to be an allowance of \$1 a day to cover all expenses of students in these various institutions, which, of course, is in some respects a nominal allowance, designed to meet the actual expenses to be incurred by the institution.

Senator THOMAS. That is exclusive of board for students?

Senator ROBINSON. No; for subsistence. I have a letter on my desk to that effect.

Senator PENROSE. It seems to me you entirely overlook the enormous appropriations made by State legislatures. In Pennsylvania

three-quarters of the revenues of the State go to charitable and educational work.

Dr. LINDSAY. Pennsylvania is quite an exception in that respect. Pennsylvania does give a very large appropriation for charitable work; not so much for educational work, except for the public schools.

Senator PENROSE. It gives the University of Pennsylvania quite a large sum every year.

Dr. LINDSAY. Yes; but I think relatively to the total income of the university, it is not by any means supporting the university. Of course, there are many States where they have State universities supported entirely by taxation. The enormous burdens of the increased taxes, the money the Government must have, will have to borne by private wealth, and that will diminish the ability of people to contribute to these things, inevitably; that you can not avoid. Therefore it seems all the more important that if you can, by a wise provision of law, encourage rather than discourage people making further sacrifices voluntarily to support these public institutions of education and charity, it would be a wise thing to do.

I want to say particularly that this will be a very small financial sacrifice on the part of the Government. You will lose very little revenue in proportion to the great gain you will get from stimulating these bequests and legacies.

Senator ROBINSON. Have you any figures as to how it will affect the bill?

Dr. LINDSAY. No. You can not get figures on it. I have conferred with officials of the Internal-Revenue Bureau and the Treasury Department, and they all say that their estimates of the returns from estate taxes are only guesses. They can not tell what proportion of the bequests last year were bequests to charitable and educational institutions. But you will see here in the report of the House Ways and Means Committee that the estimate is that approximately \$50,000,000 were received from the estate taxes. They estimate that with the increased rates in this proposed bill, that will increase to \$75,000,000, and that for the first full year under the new rates proposed here they will get \$110,000,000, and that ultimately they will get as much as \$140,000,000. Those are mere guesses, but those are the totals of the estimated returns.

Senator DILLINGHAM. What will those totals cover coming from the estates?

Dr. LINDSAY. The revenue from the Federal estate tax.

Senator DILLINGHAM. I understood that.

Dr. LINDSAY. That is the tax on all estates collected during the fiscal year. Those are the estimates of the revenue to be expected from that tax.

Senator DILLINGHAM. I did not know but what you could tell me what the details of the taxes were, that is, the nature of the tax on estates.

Dr. LINDSAY. The tax is a graduated succession tax on the net estates of all decedents during the year.

Senator GERRY. I think I can probably answer your question, Senator. The tax is on the net estate instead of on the beneficial interests. In most States the tax is either on the beneficial interest or a small

amount on the net estate, and then a surtax on the beneficial interest. This tax is on the entire net estate.

Senator DILLINGHAM. It does not relate to the benevolences that he was discussing particularly.

Dr. LINDSAY. It does, in this way: The tax is to be paid after the deductions. There are certain deductions allowed in the law—administrative expenses, funeral expenses, debts of the decedent, and a lump-sum deduction of \$50,000, which is intended to protect the interests of the immediate wife and children. After that the net estate tax is a graduated tax upon that. That has to be paid as the first claim out of the estate. Therefore, it comes as a burden upon the residual estate. If the residual estate is wiped out, then any bequest out of the residual estate disappears.

The CHAIRMAN. You would only have to pay a tax on a bequest for charity in case there was no residual estate. First, you pay the debts, the taxes, and then you pay the legacies and the bequests.

Dr. LINDSAY. No; you first have to pay the Federal estate tax.

The CHAIRMAN. No; you do not have to pay the Federal estate tax first. You pay the legacies first, and if there is a residuum, you pay the whole taxes out of the residuum.

Dr. LINDSAY. I beg pardon, Senator.

The CHAIRMAN. That is the way I understand it.

Dr. LINDSAY. That is not the way it is administered. I just had to administer an estate. The executor is not allowed to pay a single legacy until he has paid the estate tax.

Senator SMOOT. No; no legacy can be paid until the taxes are paid.

Dr. LINDSAY. The debts can be paid, but nothing else.

Senator ROBINSON. That must be the rule. Otherwise the legacies might be paid and the tax not paid.

Dr. LINDSAY. Yes.

The CHAIRMAN. My theory was that the tax would be paid out of the legacies, of course, if there is no residuum, but if there is a residuum, then the tax is paid out of that to the relief of the legacies.

Dr. LINDSAY. To the relief of the legacies, yes.

The CHAIRMAN. That is the point I am making. It is only a contingent case when the legacy left to charity would have to pay the tax.

Dr. LINDSAY. But the point I am arguing for is this, particularly in the case of hospitals. The common and ordinary thing that happens, as I think most lawyers who have to do with the settlement of estates will tell you, is that a man leaves a small legacy or bequest to a hospital out of his residual estate, after he has made his specific bequests. He says, "All the rest of my estate shall be divided equally between the Metropolitan Hospital and Columbia University," we will say. Of course, the Metropolitan Hospital and Columbia University will pay the entire tax, because their interests will be reduced by the amount of the tax.

Senator PENROSE. You can take by way of illustration the Sterling bequest to Yale College.

Dr. LINDSAY. Yes, that is a very good illustration.

Senator PENROSE. The Government takes pretty near half of it.

Dr. LINDSAY. The Government will take pretty nearly half of it.

Senator SMOOT. If the program as so many, many wish is carried

out, that is, to take all of it over and above \$25,000, then they would not get anything. Many, many people in this country believe that every dollar of it ought to be taken by the Government over and above \$25,000.

Dr. LINDSAY. I think the principle of an inheritance tax is a sound principle, and I think also we ought to keep in mind that this provision is probably going to be a permanent provision of law. This is not a temporary tax. This is an estate tax, and therefore it is all the more important that we should consider now the effect in the long distant future of discouraging, or making impossible, the support of public institutions for public purposes by private benevolence.

Senator GERRY. Professor, if the tax were on the beneficial interest instead of the entire net estate, or the surtax was on the beneficial interest, would not that to a certain extent aid what you are contending for?

Dr. LINDSAY. To a certain extent that might relieve the beneficiaries under the residual estate, because they carry not only their share but they carry their share of the specific bequests.

Senator SMOOT. They do not carry anything if there is enough of an estate to pay all that they give the university and pay the tax besides. If there is not enough to pay the tax then, of course, it falls upon the university or any other institution.

Dr. LINDSAY. Yes. But, Senator that is the point I am insisting on most here. That is true of a great many cases, as you have stated. But there are also many cases where a proportion of the residual estate is given, or the whole residual estate, as Senator Penrose suggested a moment ago, goes to a beneficial purpose. Therefore, that interest is reduced by the amount of the tax on the whole net estate.

Senator SMOOT. There is no doubt about it.

The CHAIRMAN. Dr. Lindsey, I was not incorrect in the idea I had a little while ago, and I do not think I was quite understood by you and some members of the committee. The point I have in mind is this, that if the testator desires to do so he can make a specific bequest in favor of a charity, just as he can make a specific bequest to one of his kinsfolk. If he wants this money to go to a charity without reference to whether he has a residuum or not, he can make a specific bequest to that charity. If he does that, and if there is enough money to pay that and his other specific bequests, and there is a residuum left, the tax would have to be paid out of the residuum in that case.

Dr. LINDSAY. Yes.

The CHAIRMAN. So that very likely the testator can control that situation, provided he does not specifically devise all of his estate.

Dr. LINDSAY. Yes.

Senator THOMAS. I think the understanding which we had of your statement was that the legacies be actually paid over before the expenses of administration.

The CHAIRMAN. No, I did not mean that.

Dr. LINDSAY. The chairman is entirely correct in that statement, that if a man has a large enough estate he can make a provision for a specific bequest, and specify that that shall go free from all tax, and if the rest of his estate is large enough to pay the tax he can

give a charity or educational institution a specific sum which would not be reduced by the tax.

Senator SMOOT. The Government sees, though, that they are going to get the tax.

Dr. LINDSAY. The Government gets the tax, and if the tax is very large, as it is under these new rates, and the executor has to sacrifice property, perhaps, to pay it, even within the extended time that is allowed in this bill, it sometimes is going to be very difficult to settle an estate and pay the Government tax and leave specific bequests without being reduced in some way by the amount of the tax.

Senator JONES. Professor, to what extent have the educational institutions of the country been affected by the war, so far as their attendance is concerned?

Dr. LINDSAY. Most of them have been shot to pieces, as we say.

Senator JONES. If that be the case, for war purposes why would it not be advisable for us to try to get a revenue from the war and take care of these institutions after the war is over?

Dr. LINDSAY. That has been suggested. But you must remember, in the first place, that these educational institutions are only a part of those for whom I am speaking. The hospitals, the charitable institutions, are under greater pressure for work now than they were before the war.

Senator JONES. As I take it, the Government is going to establish a very great number of hospitals.

Dr. LINDSAY. Yes.

Senator JONES. On its own account.

Dr. LINDSAY. Yes. It is also calling upon all of the privately endowed hospitals to do their utmost to cooperate with the Government, and supplement what the Government can do itself. Surg. Gen. Gorgas wrote a letter to the House Ways and Means Committee in which he expressed his earnest desire that this help be given as a necessary means of cooperating with the Government in the matter of hospitals.

Senator JONES. Would you suggest, then, that we make a distinction as between hospitals and colleges?

Dr. LINDSAY. No; because I think that the colleges have large plants that must be kept up. They are everywhere being devoted to war purposes. At Columbia University, for example, where I happen to be, we have devoted three buildings this year to a Government barracks, practically, and we turned over before that other buildings, I think certain chemical laboratories have been turned over to the Government work. I do not know the details of how the Government is going to meet the support of that work. I should be very much surprised if that is not going to cost the institution more than it will get from any compensation the Government may pay for the use of those buildings. These plants have to be kept up whether there are students there or not. In many cases, in many institutions, there are students coming, not the regular class of students, but there are women attending some of the colleges where women are admitted, and there is an educational work to be done there.

Senator JONES. Do you not think it advisable for the Government to directly compensate for that accommodation, rather than leave it to the haphazard hope of getting something through legacies and bequests?

Dr. LINDSAY. I think it will be very much more expensive for the Government to do it that way, and it will be a departure from our traditional policy, which has worked so successfully that it has been one of the things we have boasted most of in America.

Senator JONES. This war has caused several departures from the ordinary course of conduct.

Dr. LINDSAY. I know it has.

Senator GERRY. Professor, are not your medical schools running very nearly normal?

Dr. LINDSAY. Yes; as far as number of students go.

Senator ROBINSON. Reference was made a while ago to what the Government proposes to do to compensate the institutions where instruction is to be had for soldiers. I made the statement then as to my understanding of the matter, and with your permission I will read into the record just a few lines from Philip H. Driscoll, major of infantry, United States Army, executive officer, in which he says (reading):

The present S. A. T. C. schools are to be covered by temporary contract which must be signed by the Jonesboro Agricultural College. This temporary contract will provide for \$1 per day per man, and covers subsistence and quarters, and the average yearly tuition divided by 270 to pay for this. Then this allowance of \$1 per day. Barracks will have to be erected by the institution and paid for by it.

I think that confirms the opinion I expressed.

Senator SMOOT. The only thing I had in mind, I will say to the Senator, was as to what the Government actually paid. The Government pays the \$1 a day for the purpose named. The Government also furnishes the uniforms for every boy who goes to this school.

Senator ROBINSON. But out of this subsistence and quarters must be provided, which is contrary to the statement made by some Senator.

Senator THOMAS. I was informed yesterday by a student from the Drexel Institute that he was notified that he would be required to enter the service and wear a uniform if he expected to enjoy the privileges of that school longer, and that upon entering the service, he would receive the pay of a private, \$30 a month, his uniform and has subsistence. That letter, I think, is perfectly consistent with that statement. The institution gets, in addition to that, \$1 a day from the Government.

Senator SMOOT. For that purpose.

Senator McCUMBER. Then the Government furnishes the subsistence after all.

Senator ROBINSON. No.

Senator THOMAS. I think so. I base that upon the statement to me.

Senator ROBINSON. The \$1 a day that the Government pays to the institution must cover the subsistence of the student, his tuition, and the cost of providing barracks, whatever that may be. If barracks are not already provided by the institution and available, an arrangement may be made, and all that is charged back to the institution at the day rate per man.

Dr. LINDSAY. If that is all the institution would get, I do not think the larger institutions will be able to furnish that without an additional cost upon their own funds.

Senator ROBINSON. That is undoubtedly true.

Senator PENROSE. Is there any evidence that that applies to all educational institutions?

Senator ROBINSON. No, sir. The statement is as to these training schools that can be availed of now. That temporary contract has to be made. It is probably uniform, and it is a temporary contract which may not be changed to meet future conditions. We are speaking about the arrangement that the Government has made in taking over these schools.

The CHAIRMAN. Are you through, Mr. Lindsay?

Dr. LINDSAY. Yes. I should like to add to this a reference to the fact that I presented to the Ways and Means Committee, and there are printed in part 1 of the hearings before the Committee on Ways and Means on the proposed revenue act of 1918, pages 887 to 910, a good many documents and letters in support of the statement I have made here. I do not think it is necessary to introduce them into your record.

Senator SMOOT. I think we have all received letters similar to the one you put in the record in the House hearings.

Dr. LINDSAY. I would like to call the attention of the committee to another matter, not with respect to the estate tax, but with respect to the income tax.

In the draft of the new revenue act there has been a change made, on page 16 of House bill 12863, subdivision 11, in the provision that is now a part of the present law, which was introduced by the provision adopted by the Senate and accepted by the conference last year with respect to the income tax. There has been a change made in the language of this exemption:

Contributions or gifts made within the taxable year to corporations organized and operated exclusively for religious, charitable, scientific, or educational purposes.

The present law reads, "to corporations or associations." It would seem that this change would limit the benefit that was granted in the act of last year somewhat to incorporated societies. It was not the intention to give that benefit only to incorporated institutions, but also to include societies and association not incorporated. There is one exception, however. The change is not made, and therefore this paragraph, as it now stands, is hardly consistent.

The CHAIRMAN. If you will turn to the first page you will find the term "corporation" is defined:

The term "corporation includes associations, joint stock companies, and insurance companies, as well as private corporations.

Dr. LINDSAY. Then that covers the point very well.

The CHAIRMAN. That includes, necessarily, associations.

Dr. LINDSAY. Yes.

The CHAIRMAN. Is there any other point you want to call to our attention?

Dr. LINDSAY. No, sir. I thank you very much.

The CHAIRMAN. Mr. Hunt, we will hear you now. Before you begin, is there any other representative of the industry you are speaking for who desires to be heard?

MEDICAL PREPARATIONS.

STATEMENT OF MR. ATHERTON N. HUNT, 84 STATE STREET,
BOSTON, MASS.

Mr. HUNT. I think it is possible some other representatives desire to be heard in regard to this section. I am not acting in co-operation with them, neither am I antagonizing any suggestion they have to make, so far as I know.

The CHAIRMAN. We have made the suggestion here, and I think our time would be greatly conserved if it were followed, that where there are several representatives of the same industry, that they get together and agree that some one or two, and not more than two, shall speak for the industry. We can not have indefinite hearings, you know. There might be 20 men desiring to speak for the same industry, and it would take too much of our time. If there is one other, that would place a limitation upon your time. If you speak solely for the industry, we could give you more time.

Mr. HUNT. Mr. Chairman, it was my purpose to speak for the American Association of Pharmaceutical Chemists, a nation-wide association embracing practically all of the pharmaceutical manufacturers. There are, of course, the drug associations, and other branches of the trade, that perhaps will look at the matter from a different angle from the angle taken by my clients. I desire to present briefly to the committee one phase only.

The CHAIRMAN. How long will you want? We have to fix some limit of time, or we will not begin to get through these hearings in the time we have set for them. You are here, and here is another gentleman who has asked to be heard representing the same interests. How much time will you want?

Mr. HUNT. I shall want only a few minutes.

The CHAIRMAN. Very well. Go ahead. We will give you 15 minutes.

Mr. HUNT. The American Association of Pharmaceutical Chemists, Mr. Chairman and gentlemen of the committee, is composed of 40 or 50 manufacturing corporations and firms making medicinal products, and the difficulty with the situation of the proposed act from their point of view is this. I am not here for the purpose of objecting or protesting against taxation as such. My whole duty in the matter is to call attention to what appears to us to be unjust taxation, not intended by Congress, and that unjust taxation is a matter of history and inheritance, the language adopted in the proposed act being a relic of the past, and not being applicable, as we believe it, to the present situation as now interpreted by the Commissioner of Internal Revenue.

I took the liberty of sending to each member of the committee, within 48 hours, a copy in print of a brief which has been prepared.

The CHAIRMAN. Will you give that to the reporter for incorporation in the hearings?

Mr. HUNT. I will present a copy. In that brief I have called attention to what appear to be to us two necessary changes in the statute. The old section 600h of the 1917 revenue law has been reproduced in part in section 908a, subsection 2, page 58 of the printed abstract of the proposed bill. I will not take my time to read the

section, but I will call attention to the words "or trade-mark," which appear in connection with various other specifications; and words "or as remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body." Those two phrases are added to a lot of other phrases describing, in the main, proprietary articles or medicinal preparations.

As I conceive it, Congress meant, and means now, to tax proprietary medicines. It has been a consistent policy of Congress for 60 years in emergency taxation measures to tax proprietary medicines. That phase of it I do not care to discuss. That I gladly leave to others. Whatever my personal feelings may be about it, I believe that to be the settled policy of Congress.

Those two phrases, however, have brought about a curious situation. The Commissioner of Internal Revenue has interpreted those words "or trade-mark" to mean that any pharmaceutical manufacturer who uses what I call a general business trade-mark; that is, a trade name or trade symbol, that is applicable to all of his goods, whatever they may be—not a specific trade-mark claiming any proprietary rights of any kind—subjects the goods sold under it to taxation. I am informed, after conference last night with the solicitor of the department, that possibly the department will recede from the decision which was rendered to me on this particular phrase. I emphasize it now because, whether the ruling of the department is right or wrong makes no difference in our contention as to these two phrases. The phrase "or trade-mark" simply creates this confusion, and laid foundation for the opinion that was sent to me early in this year that such matters were taxable. I think the department is about to recede from that, under the advice of the solicitor.

The other phase of the matter is this phrase, "or as remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body."

That phrase is, verbatim et literatim, an inheritance from the past. It is the same phrase used in the act of the Civil War, in that of the Spanish War, and in that of last year—every emergency measure. When all of us were boys we were familiar with the kidney cures and consumption remedies and rheumatic specifics, and things of that kind, special medicines which had designations of that kind, that were sold as remedies or specifics for some particular disease. I apprehend that that is what Congress meant by the phrase in 1860 and in 1898 and in 1917. But the Commissioner of Internal Revenue says that what Congress meant by that phrase "or remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body," is that where a pharmaceutical manufacturer has on his label therapeutic limitations; that is, any of the ordinary things we see printed on the bottles, such as "Fever. (For children.)" I have put in what I meant to be some horrible examples, on page 18 of this brief, which I have submitted to the members of the committee. One of them is "Coryza Compound, No. 4. Dr. Kenyon." Of course, all of these medicinal remedies are the result of formulas discovered and approved by doctors years ago. Every one of these formulas on which these thousands of medicinal products are manufactured originated in the mind of some healer, some physician or surgeon, and has come down through approval and experience, until it has received the approval of the profession.

This coryza compound is very old. It is manufactured by every pharmaceutical manufacturer in the country.

Senator LODGE. It is open to the public?

Mr. HUNT. It is open to the public, Senator, and nobody claims any proprietary rights in it whatever.

Senator THOMAS. Let me see if I understand you. The construction given by the commissioner to this clause is so broad that it includes nonproprietary as well as proprietary medicines?

Mr. HUNT. That is the point which I am about to reach. The result of these two rulings on the words "or trade-marks," and "or as remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body," is that the entire distinction which has been preserved through all these years, and that Congress, I believe, meant and still means to preserve, between proprietary remedies and medicinal products, is entirely abrogated.

There seems to be a settled policy of taxing proprietaries. I can not persuade myself that Congress ever meant to tax medicines in general, and add that burden to the sick.

Take, for example, the particular trade I represent. It is the trade which manufactures the ordinary working tools of the physician, the physician throughout all the country who dispenses his goods. The National Drug Company, for whose representative, Mr. Pratt, I am now speaking, with the other members of that association, I am told has over 13,000 open accounts on its books. Those physicians are scattered from Eastport to the Mississippi River, and many of them are miles and miles from a prescription desk, and they are compelled to carry the medicines which they dispense at the bedsides of the sick, and those medicines are the ordinary working tools of the physician, and are the things which I am suggesting Congress never meant to tax. But under the act as it now stands the commissioner says, they are subject to the tax of two per cent under the act of 1917, and under the present act were supposed to be subject to a tax of 10 per cent, and under the act as now contemplated are now subject to a tax of more than 10 per cent, because one cent in ten runs it to over 10 per cent.

That tax on general medicinal products is prohibitive, for this reason: The trade can not absorb any such tax. Proprietary medicines, of course, are sold upon a monopolistic basis. I will let the representatives of the proprietary medicines speak about that. But certainly they are sold upon a monopolistic basis—almost every one of the manufacturers for whom I speak, as well as the proprietaries. There may be part of their products proprietary, but the great part is general medicinal products. But the general medicinal products are sold upon a very close competitive market, and sold by salesmen who travel all throughout the country to see the different doctors. That tax can not be paid by the manufacturer on any present scale of prices. It seems a kind of fatalism that surpasses even the Oriental, to pass that tax to the doctor, who is struggling to save human life. We do not want to tax the patient for his inadvertence in being sick. There is no place to put the burden. The manufacturer can not carry it and stay in business, the sick man ought not to carry it, and the doctor can not carry it without increasing his charges.

The CHAIRMAN. The bill does require the sick man to carry it, does it not?

Mr. HUNT. I think not.

Senator THOMAS. It will be passed on to him.

Senator SMOOT. They can not charge any more than they are charging now, any how.

Mr. HUNT. What I meant to say was that it was entirely impractical to pass the tax along, because you can not pass it along. It will not go.

Senator THOMAS. That is one of the taxes I want to find. I am looking for that kind of a tax, that can not be passed along.

Mr. HUNT. And the manufacturer can not pay it.

Senator TOWNSEND. Can not the physician increase his charges?

Mr. HUNT. The physician ordinarily dispenses that medicine at the bedside of the sick without addition charge, and my feeling is that the physician can not increase his charges. I think it would create such resentment throughout the community—

Senator TOWNSEND. Do I understand the physicians have not increased their charges since the war opened?

Mr. HUNT. Not in connection with medicines, so far as I know. I am now talking about the possibility of a physician increasing his charges because of the medicine which he dispenses at the bedside.

Senator SMOOT. The medicine is such a little part of what he charges that it does not amount to anything.

The CHAIRMAN. You are not talking about the medicine sold by the dealer but sold by the physician?

Mr. HUNT. In the main. That is very little of the product of the Manufacturers' Association which I represent.

The CHAIRMAN. I notice in the bill here that you are talking about it requires that a stamp be affixed to the article by the vendor, the cost of which shall be reimbursed to the vendor by the purchaser.

Mr. HUNT. That is one of the alternative methods of collection. That is part of the machinery of collection. Whether or not that machinery can be made to operate in the case of these medicinal remedies is the point I was trying to explain. I do not believe it can be made to operate, because what we are under now, under this ruling, is this, that we can put upon our labels "Made by X Y Z" we can throw away all our general trade-marks and use a legend like that "Made by A B," and he can wipe off the labels, obliterate from all of our labels the scientific therapeutic indications that are a guide to the mind and hand of the practitioner and not pay any tax. Under the ruling of the commissioner, if we take off those therapeutic indications, we do not pay any tax. My characterization of that situation is that it is too absurd for argument, that the therapeutic indications that are ordinarily now printed on additional labels—

Senator LODGE. You mean the formula?

Mr. HUNT. Fever, heart tonic, cardiac stimulants, conjunctivitis. When we get a cinder in the eye we get what we call a sore eye. The doctor calls it conjunctivitis. We all know that boracic acid is what goes into all eyewashes, and the doctor who is reaching for eyewash does not want a cardiac stimulant, and anything on the label that guides his hand immediately to what he wants, whether it is a label showing the manufacturer, the origin of the article, or whether it is the trade-mark of the house with which he wants to deal, or whether it is the name "conjunctivitis" or "cardiac stimulant," or something of that kind that he is after, the thing that guides his hand to that bottle in his bag quickly is the thing that is wanted. It may make

a difference whether the remedy is administer at 4.30 or 4.35. The ruling of the commissioner, and the statutes together, now mean that if we take off all that safeguard of the general public and of the doctor and the nurse, and throw it away, and throw away our general business trade-marks, we escape the tax, but if we put them on and give the public the benefit of those trade-marks, that is, the hall-mark of respectability attached to these medicines, and give the doctor and the patient the benefit of the therapeutic indications, which are based on experience, and not the proprietary name—if we use those we are subject to the tax.

Senator LODGE. Mr. Hunt, this whole section is drawn to cover "medicinal preparations, compounds, or compositions (not including serums and antitoxins) upon the amount paid for any of the above as to which the manufacturer or producer claims to have any private formula, secret, or occult art for making or preparing the same." They do actually rule in the Treasury that if the Squib Manufacturing Co., for instance, put out bicarbonate of soda and put their name on it it is taxable as a proprietary medicine?

Mr. HUNT. I did not follow your question.

Senator LODGE. You spoke about the trade-mark.

Mr. HUNT. For example, the trade-mark of a concern for which I am general counsel and director prints a representation of the Sphinx. It is printed on the boxes, printed on all the cartons and labels and everything else, and the concern has been known for years as a manufacturer of Sphinx pharmaceutical articles. The commissioner rules that because that has the Sphinx on it it is taxable. I think the commissioner is about to recede from that ruling, because I understand the solicitor of the department has rendered an opinion that that is not what it means.

Senator LODGE. That is not quite my question. Suppose Mr. Squib makes a peculiarly good quality of an article, and they put on it "Squib's Bicarbonate of Soda." Does the department hold that that is taxable?

Mr. HUNT. If you say "Squib's Bicarbonate of Soda," that is the possessive, if you claim anything which indicates you have a superior way of making it from anybody else, if you claim any occult or peculiar right or proprietary right or right of property, or claim of any kind that your remedy is better than somebody else's, that is, that it is not bicarbonate of soda as we know it, but an extra quality of bicarbonate of soda, that is, the instant you claim it is not what it says, it is taxable. But if you say "bicarbonate of soda" or "sulphate of quinine," or any of these things, and put on a general trade-mark like, for example, the entwined hearts of the Hart Bros., the red cross of Johnson & Johnson—those things have been in difficulty during this last year.

The CHAIRMAN. Did you not tell us a few moments ago that you thought, after consultation between you and others, that the department would change this ruling in regard to that matter?

Mr. HUNT. I think the department is going to recede from that position. But what I am about to say is this, that the appearance of those words in the section made that misunderstanding, and all this controversy possible, and the words are of no value whatever in the section, because I defy the imagination of anybody to conceive of

anything which is included in those words which is not included in the other—

The CHAIRMAN. Suppose the words are stricken out, and the department changes this ruling. What other point have you?

Mr. HUNT. If those words are stricken out, and the department changes this ruling, the other point is, "or as remedies or specifics for any disease," etc. Those words were put in there 60 years ago, as applying to kidney cures and consumption remedies. But they are now obsolete, because the Pure Food and Drugs Act makes it unlawful to sell anything which says "Kidney cure." You can not sell a consumption remedy now without being prosecuted, and those two items, as I view it, were meant to apply to those specific things, and not to remedies, because if you take the word "remedy" in its broadest possible sense, you find that the definition is as stated in the brief. The instant you take the broad definition, as the commissioner says we must, we would land with general medicinal products. The definition of "remedy" as contained in this brief, as taken from Webster's International Dictionary, is (reading):

First, that which relieves or cures a disease; any medicine or application which puts an end to disease and restores health.

Second, that which corrects or counteracts an evil of any kind; a corrective; a counteractive preparation; cure.

Can anybody conceive of anything used in medicine or surgery that does not come within that definition "remedy" as used in its broadest sense? If we use "remedy" in its broadest sense, we mean general medicinal products, and I respectfully submit to this committee, as I have in my brief, that that is not what Congress meant, and I do not believe that Congress means it now. If that is what Congress does mean now, that is the thing which I am here to protest against—not against taxation, but against taxation which is unjust in taxing as luxuries this great class of general medicinal products which are imperative necessities, as imperative necessities as food to eat or water to drink, the medicine that protects our families.

The CHAIRMAN. Then you want us to strike out the words "or trademark" and "or as remedies or specifics for any disease, diseases or affection whatever affecting the human or animal body"?

Mr. HUNT. Yes, Mr. Chairman.

Senator THOMAS. Do you propose any substitute for those words?

Mr. HUNT. No, Senator, because my contention is that that phrase "or trademark", as well as the other, is entirely superfluous and obsolete, and should be stricken from the statute, because whether the ruling of the Commissioner of Internal Revenue is right or wrong makes no difference, except to point out and emphasize the necessity of having this statute in such clear shape that there can be no misconception of it either by the Department of Internal Revenue or by any one else.

Senator McCUMBER. Did I understand you to say that under the pure food law you are prohibited from selling an article denominated "Consumption Cure" or "Kidney Cure"?

Mr. HUNT. Yes, in interstate commerce.

Senator McCUMBER. On what theory? The law does not prohibit it.

Mr. HUNT. It is a claim that can not be sustained that it comes under the misbranding section.

Senator McCUMBER. In other words, you have to prove that it is a cure?

Mr. HUNT. Yes. If you say "consumption cure", you are held to defraud the public.

Senator McCUMBER. That there is no such thing?

Mr. HUNT. That there is no such thing as a consumption cure, and that a remedy, in the sense we use the word, is a thing which is used to alleviate disease. It may or may not be successful.

Senator PENROSE. As a matter of fact, that regulation is largely ineffective, because these proprietary articles do contain a long list of complaints which they are said to relieve.

Mr. HUNT. I apprehend that most of the proprietary remedies do have some virtue. I presume there must be some virtue in all of these things.

Senator PENROSE. It has been said to one of my associates that many of them relieve the craving for alcohol.

Mr. HUNT. I think that may be so. However, of course, the medicinal trade is a peculiar one in that respect, because it requires high percentages of alcohol to maintain in solution the different drugs, especially the alkaloids. There has been much question before this committee, especially about Jamaica ginger, and I doubt now if many people outside of the profession understand why Jamaica ginger has in it such a large percentage of alcohol.

The CHAIRMAN. I think the committee understands you. I think we have given you very liberal time. If there is any other statement now you want to make we will be glad to bear that, but I think we understand what you have been saying about this particular phrase. When we take that up, if we see proper, we may confer with the department about the construction of the department on this section.

Mr. HUNT. There was only one other phase of the matter I wanted to speak about. There has been submitted, prior to this time, by general counsel for the American Association of Pharmaceutical Chemists, with whom I am associated, a memorandum calling attention to the distinction between drugs which are dispensed by physicians and drugs which are sold to the laity. If the committee feel that for any reason those words can not be stricken from the statute, I think that careful consideration should be given to the alternative suggestion, of discriminating between the things dispensed to physicians and things sold to the laity. I believe, and I respectfully submit to this committee, that the way to reach this thing, the way to clear it up without friction and to put everything on the basis where it should be sold, is to strike out the word from the statute. But I do not want to retire without bringing that other suggestion to the attention of the committee for just a moment, to make that distinction between the things which are dispensed or used under the direction of physicians and surgeons and veterinarians, and the things which you and I, Mr. Chairman and gentlemen, all know as proprietary medicines, the things which are sold to the laity, and which are sold on request off the shelf.

Senator PENROSE. Did you have an opportunity to submit your objections to this phraseology to the House committee?

Mr. HUNT. I am delighted, Senator, to have you ask that question, if I may have time to answer it. The matter was brought to my attention professionally very late, and I obtained a conference with

Mr. Kitchin, of the House Ways and Means Committee. He told me that I had better refer the matter at once to the chairman of the subcommittee, Mr. Hull of Tennessee. But he said, "I want to say to you frankly that even if Mr. Hull's subcommittee reports in favor of these changes, I do not believe that we will take the bill to pieces at this stage, because it is substantially in print, ready to come out of the committee. The most feasible plan for you to adopt is to take your suggestions before the Senate Finance Committee, when the bill comes to them, and have it dealt with in conference if Mr. Hull's subcommittee favors the suggestion." The reason he gave me was that it was so late, and it was very late. It was not until this month, about the first of the month, that I was retained to present this to Mr. Kitchin and to Mr. Hull. I think the attitude of Mr. Kitchin and Mr. Hull was favorable, so far as I could view it. But they did not wish to obstruct the passage of the bill at that time, because it was printed and ready to come out of the committee. That was the fault, perhaps, of my clients in not bringing it to their attention earlier, rather than the fault of the committee.

(The brief submitted by Mr. Hunt is here printed in full, as follows:)

BRIEF ON BEHALF OF AMERICAN ASSOCIATION OF PHARMACEUTICAL CHEMISTS
AND NEW ENGLAND DRUG MANUFACTURERS' ASSOCIATION.

SECTION 600 (H) WAR-REVENUE LAW, OCTOBER 3, 1917.

"(h) Upon all pills, tablets, powders, tinctures, troches or lozenges, sirups, medicinal cordials or bitters, anodynes, tonics, plasters, liniments, salves, ointments, pastes, waters (except those taxed under section three hundred and thirteen of this act), essences, spirits, oils, and all medicinal preparations, compounds, or compositions whatsoever, the manufacturer or producer of which claims to have any private formula, secret, or occult art for making or preparing the same, or has or claims to have any exclusive right or title to the making or preparing the same, or which are prepared, uttered, vended, or exposed for sale under any letters patent, or *trade-mark*, or which, if prepared by any formula, published or unpublished, are held out or recommended to the public by the makers, venders, or proprietors thereof as proprietary medicines or medicinal proprietary articles or preparations, or as *remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body*, and which are sold by the manufacturer, producer, or importer, a tax equivalent to two per centum of the price for which so sold."

The italics are ours, and attention is particularly directed to the two phrases emphasized.

PROPRIETARY MEDICINES DISTINGUISHED FROM GENERAL MEDICINAL PRODUCTS.

Medicinal products are divided by a very sharp line of distinction into two great classes.

First. Proprietary medicinal articles or preparations prepared, manufactured, and sold under some claim of exclusive proprietary right.

Second. General medicinal products in which no exclusive proprietary right is claimed, manufactured and prepared according to well-known scientific formulae proved by experience and demonstrated in practice.

Proprietary medicinal articles or preparations included in the first class are manufactured and sold on the basis of an exclusive monopoly. General medicinal products, other than proprietary medicinal articles or preparations, are sold on the basis of a close competitive market. The general medicinal products include the ordinary scientific medicinal preparations or articles prescribed, dispensed or used by or under the direction of physicians or surgeons. In the main, proprietary medicinal articles or preparations find their market among the general public apart from the direction of the medical profession. Atten-

tion is directed to these distinctions not in any spirit of disparagement toward proprietary medicinal articles or preparations but merely to point out the two lines of cleavage between the great classes of medicinal products.

PURPOSE OF CONGRESS.

Under the above section it is apparently the settled policy of the Congress to tax proprietary medicinal articles or preparations. This is not a new idea and is consistent with prior statutory enactments. The statute does not purport to tax general medicinal products.

NO INTENT TO TAX GENERAL MEDICINAL PRODUCTS.

The language of section 600 (*h*) necessarily implies the intent of Congress to tax only proprietary preparations, because if the intention of Congress had been to tax medicinal products generally, the care displayed in defining the various classes of proprietary medicinal articles or preparations would have been unnecessary. The only object in defining the various kinds of medicinal preparations in which proprietary rights are claimed must have been to distinguish the proprietary medicinal articles or preparations taxed from the general medicinal products which were not taxed. If the Congress had intended to tax medicines in general it would have used apt language. The present language would have been without justification or excuse.

REASON FOR THIS BRIEF.

Under the above section, as the two phrases emphasized are interpreted by the Commissioner of Internal Revenue, a manufacturer of pharmaceutical products who uses a general trade-mark or prints therapeutic indications on his labels must pay a 2 per cent tax on his gross sales and under the proposed amendment must pay a 10 per cent tax not on his proprietary products alone but on his gross sales.

Such a result would be a public calamity.

PROPOSED MODIFICATIONS SECTION 600 (*h*).

On the assumption that the Congress meant to tax and now means to tax only proprietary medicinal articles or preparations and did not intend and does not now intend to tax general medicinal products, it is submitted that the words, "or trade-mark" appearing after the words, "under any letters patent," and the words, "or as remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body," appearing after the words, "proprietary articles or preparations," have no proper place in the statute and should be stricken therefrom.

GENERAL TRADE-MARK DISTINGUISHED FROM SPECIFIC TRADE-MARK.

There are two great classes of trade-marks:

First. General or business trade-marks, otherwise known as trade names.

Second. Specific trade-marks.

These two classes of trade-marks differ from each other in character, use, purpose and effect.

Difference in character.—Such trade-marks differ in character, in that a specific trade-mark is applicable to one or more articles of a particular character, while a general business trade-mark is applicable to all the merchandise, however varied in character, held out for sale by the business house entitled to use it.

Difference in use.—Such trade-marks differ in use, in that a specific trade-mark, owing to its origin and character, can be used in only a very limited way, having no force nor meaning apart from the particular merchandise with which it is associated and which it is designed to protect, while a general business trade-mark is customarily used by a merchant in connection with all the kinds of merchandise in which he deals, irrespective of the kind or variety of merchandise and without regard to whether specific trade-marks may also be applicable or not.

Difference in purpose.—Such trade-marks differ in purpose, in that a specific trade-mark is intended to assert and does assert some exclusive claim of

proprietary right in the specific articles to which it is attached, while a general business trade-mark asserts no such claim and is intended to protect the owner of the trade-mark from fraud and imposition by other merchants who might otherwise deceive the public as to the identity of the manufacturer whose goods they were purchasing.

Difference in effect—Such trade-marks differ in effect, in that a specific trade-mark is a warning that the manufacturer claims some exclusive proprietary right in the article to which it is affixed and protects the manufacturer against infringement of such right, while the general or business trade-mark asserts merely the name and identity of the owner of the trade-mark and protects the public against purchasing other goods designed to be sold as his.

EXAMPLES OF TRADE-MARKS CLASSIFIED.

As examples of a general business trade-mark, I would cite:

"In Er Seal," the trade-mark of the National Biscuit Co.

"Necco," the trade-mark of the New England Confectionery Co.

The trade-mark of the Gorham Manufacturing Co., the silversmiths of New York and Providence, consisting of three plaques combining an adaptation of part of the old English "Hall Mark," an anchor and the letter "G."

"Kodak," the trade-mark of the Eastman Co.

As examples of specific trade-marks, I would cite:

"Gold Medal," the trade-mark of the Washburn Crosby Co. for flour.

"Bon Ami," the trade-mark applied to the well-known cleaning preparation.

"Postum," the trade-mark applied to cereal coffee.

"Fatima," cigarettes.

"Ivory," soap.

The general business trade-mark of a pharmaceutical house used to indicate the origin of its products and not to assert any proprietary right in any special article manufactured or sold, is in reality a trade name. As such it stands for built up reputation; it is a link that connects the ultimate consumer with the manufacturer. It preserves the identity of merchandise, and, in carrying out this function, it is a device of inestimable value to the commercial world. Its use should be protected and encouraged; and the manufacturer should not be deprived of its advantages by measures of taxation which makes its use impossible.

VALUE OF GENERAL BUSINESS TRADE-MARKS.

A general business trade-mark asserts no claim of proprietary rights in the article to which it is affixed. It is only one way of announcing the identity of the manufacturer. It is a convenient and concise way of telling a purchaser that he is dealing with a commercial house with which he desires or intends to deal. Such trade-marks assume value to the vendor according to the reputation obtained for honesty, fair dealing, and excellence of product. It is a great injustice to deprive a business house of the benefit to be derived from its own reputation, from its continuity in business, or from the well-recognized quality of its products. The names of various business houses are synonyms for honesty and sincerity; and the value of a good reputation is an asset which is jealously protected by law. The law does not allow a man to steal his neighbor's business by falsely masquerading under his neighbor's name or trade-mark. The wrong perpetrated by such a fraud is just as much a wrong to the purchaser as it is to the pretended seller who is impersonated. The public relies, as it has a right to do, on the marks of identification which distinguish the products of one merchant or manufacturer from the products of another; and a theory of taxation which destroys the value or diminishes the use of general business trade-marks is a penalty for honesty and a premium established for insincerity and careless business.

THEORY OF "EJUSDEM GENERIS" AS APPLIED TO SECTION 600 (H).

First. As to the words, "or trade-mark": In the first part of the section the Congress has specified five classes of proprietary preparations, the manufacturer or producer of which claims: First, to have any private formula; second, to have secret or occult art for making, etc; third, has or claims exclusive right or title to making, etc.; fourth, which are prepared, vended, etc., under any letters patent; and fifth, which are prepared, vended, etc., under any trade-mark.

As the first four classes necessarily relate to preparations in which exclusive proprietary rights are possessed or claimed, under the theory of *ejusdem generis*, the fifth class must also relate to preparations in which exclusive proprietary rights are possessed or claimed. Therefore, the words, "or trade-mark" as they appear in the section must relate to a specific trade-mark under which exclusive or proprietary rights in the preparations designated are possessed or claimed. The various particulars recited in the statute relate to such proprietary rights and any particular included in the list of specifications must be properly interpreted to refer to something of the same general character or kind as the other particulars which are grouped with it in the same class. It is not reasonable to suppose that the Congress intended to group together five classes of preparations, carefully define four classes which related to exclusive proprietary rights and then add a fifth class, including general medicinal products, thus subverting the purpose and meaning of all the language preceding and making the definition of all classes of proprietary remedies in idle ceremony. Unless the words "or trade-mark" refer to a specific trade-mark applied to a specific article or articles in which exclusive proprietary rights are possessed or claimed, the words would alter the whole intent of the section as otherwise expressed. The rest of the language in the section completely negatives the idea that the words, "or trade-mark" were ever intended by the Congress to mean a general business trade-mark used for the purpose of identifying the maker or manufacturer.

Second. As to the words, "or as remedies or specifics," etc. In the latter part of the section the Congress has specified three classes of proprietary preparations which are held out or recommended: First, as proprietary medicines; second, as medicinal proprietary articles or preparations; and third, as remedies or specifics for any disease, etc.

The first two classes necessarily relate to preparations in which exclusive proprietary rights are possessed or claimed. Therefore, under the theory of *ejusdem generis* as just explained, the third class must relate to preparations in which exclusive proprietary rights are possessed or claimed. The arguments set forth as to the words, "or trade-mark," apply multanidis to the words, "or as remedies or specifics," etc.

Unless the words refer to a specific article or articles in which exclusive proprietary rights are possessed or claimed the words would alter the whole intent of the section as otherwise expressed. The rest of the language of the section completely negatives the idea that the words, "or as remedies or specifics," etc., were ever intended by the Congress to mean general medicinal products sold under medicinal labels setting forth well-known and scientifically recognized therapeutic indications.

RULINGS OF THE COMMISSIONER OF INTERNAL REVENUE.

The Commissioner of Internal Revenue has ruled, however:

First. That the words, "or trade-mark" must be interpreted literally and in the broadest sense to include any trade-mark of any kind, general, business or specific, and that any medicinal products, whether proprietary medicinal articles or preparations, or general medicinal products, sold under any trade-mark are subject to the tax at present imposed.

Second. That the words, "or as remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body," must be interpreted literally and in the broadest sense to include any remedies sold under a label bearing any therapeutic indications, and that any medicinal products, whether proprietary medicinal articles or preparations or general medicinal products, sold under such a label are subject to the tax at present imposed.

These rulings have practically abrogated the distinction between proprietary medicinal articles or preparations and general medicinal products.

It is assumed that the Congress meant and now means to tax under this section only proprietary medicinal articles or preparations and the suggestions offered are submitted on that assumption. If the Congress intended the words, "or trade-mark" to include only specific trade-marks and not to include general business trade-marks, otherwise known as trade names, or if the Congress intended the words, "or as remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body," to apply only to proprietary medicinal articles or preparations and if that intent is expressed in statutory language which in any way warrants the Commissioner of Internal Revenue in ruling that medicinal products sold under general business trade-

marks or sold under labels bearing therapeutic indications are taxable within the scope of the language used, surely, in a general revision of the war revenue law, the opportunity presents itself to express the will and intent of the Congress in such language that it can not be misunderstood or misinterpreted either by the Commissioner of Internal Revenue or by declarants submitting themselves for taxation.

WORDS, "OR TRADE-MARK" NOT ESSENTIAL.

If the Congress mean and now means to tax only proprietary medicinal articles or preparations, the words, "or trade-mark" are entirely unnecessary in the section. Articles sold under a specific trade-mark asserting some claim of proprietary right are taxable under the other specifications; and the words, "or trade-mark" used with that limitation add nothing to the language which goes before. There is no medicinal article or preparation capable of being sold under such a specific trade-mark which does not come within the four classes immediately preceding. A private specific trade-mark used on a special article or articles means that the manufacturer or producer claims either a private formula, or secret or occult art, or exclusive right or title to the making, or claims to act under letters patent. A specific trade-mark must mean one of the things already referred to in the preceding language or it would have no meaning, value or commercial worth. It is submitted that the imagination can not conceive of a medicinal preparation in any way justifying the use of a specific trade-mark which does not fall within one of the classes of proprietary remedies previously defined. If, therefore, the words, "or trade-mark" are not essential to secure the taxation of proprietary articles or preparations and as now included in the section merely lead to obscuring the distinction between specific trade-marks and the general business trade-marks, the words should be omitted from the section. Unless the Congress means to tax all medicinal products, the words are superfluous. If, on the other hand, the Congress means to tax only proprietary medicinal articles or preparations, there is no reason why by the imposition of a prohibitive tax manufacturers should be debarred from the use of general business trade-marks, the identity and business value of which have been established by years of hard work and honest dealings. It has already been ruled that general medicinal products can be sold under labels bearing the legend, "Made by XYZ." It is submitted that the use of a general business trade-mark on wrappers and packages on articles of merchandise means nothing more, nor nothing less than, "made by XYZ." General business trade-marks are merely the guaranty of business reputation and assert no proprietary claim except the right of a business concern to its own name and reputation.

NATIONAL TRADE-MARKS UNDER SECTION 600 H.

Following the example set by French manufacturers and producers in adopting a collective trade-mark, "Unis-France," there are already before the Congress two bills, "the Sims national trade-mark bill" and "the Pomerene national trade-mark bill," both looking toward the establishment of a national trade-mark. If the words, "or trade-mark" remain in section 600 h as revised, does the use of the national trade-mark subject to taxation all goods uttered, vended or exposed for sale under it?

If the Commissioner of Internal Revenue is right in his ruling that the words "or trade-mark" include every kind of trade-mark, how can we reach any other result?

The absurdity of such a situation merely serves to emphasize the intent of the Congress to tax only proprietary medicinal articles or preparations uttered, vended, or exposed for sale under a specific trade-mark asserting some proprietary right in the articles to which it is attached and further emphasizes the necessity for having the manifest intent of the Congress expressed in clear and explicit terms.

THE WORDS, "OR AS REMEDIES OR SPECIFICS," ETC.

The words, "or as remedies or specifics," etc., are a survival from earlier revenue laws and as such are entirely obsolete in view of more recent legislation. Prior to the enactment of the pure food and drugs act, so-called, remedies, cures, and specifics abounded. The kidney remedies, consumption cures, and specifics for rheumatism with which we were familiar years ago are now a thing of the past, such designations being now unlawful.

If the Congress had intended to tax all remedies, using the word in its broad sense, it would have used apt language and would not have complicated the statute by such careful classification of proprietary medicinal articles or preparations. It is submitted that the Congress means to tax remedies, cures, and specifics of a proprietary nature, so far as the same may be saleable, if at all, under existing legislation and did not mean to tax all remedies.

The word "remedy" is a very broad word and is defined in Webster's International Dictionary as follows:

First. That which relieves or cures a disease; any medicine or application which puts an end to disease and restores health.

Second. That which corrects or counteracts an evil of any kind; a corrective; a counteractive preparation; cure.

The word "remedy" therefore includes every conceivable article, intended or designed to cure or alleviate disease of any kind, if we use the word in its broad sense. Such a use of the word can not be reconciled with the intent of the Congress as evidenced by the rest of the language of section 600 h. Unless the Congress meant to tax medicines of all kinds, the words, "remedies or specifics" must be interpreted as referring only to remedies or specifics in which some proprietary right is claimed. The general language and tenor of section 600 h completely negatives, however, the idea that the Congress ever meant to tax general medicinal products including such everyday household remedies as sulphate of quinine, cascara, salicylate of soda, and a multitude of equally well-known medicinal agents. The words describe no new class and add nothing to any class previously described unless they refer to general medicinal products. If the words, "remedies or specifics" as used in section 600 h are means to apply only to proprietary medicinal articles or preparations, they are not longer necessary in the statute and are superfluous. If they include general medicinal products, as the Commissioner of Internal Revenue has ruled, they subvert the meaning of the rest of section 600 h, fail to express the will of the Congress and ought not to be retained. In either case they should be eliminated from the present revision of the war-revenue law.

THERAPEUTIC INDICATIONS.

The therapeutic indications ordinarily printed on medicinal labels are not mysterious nor occult nor do they assert any claim of proprietorship. They are merely the result of experience and serve to guide the mind and hand of the medical practitioner, of the nurse, and even of the patient himself in the treatment of disease. It is a strain upon the reasoning powers to comprehend how any claim of proprietorship can be gathered from a label, on which a medicinal formula is printed and which bears the legend "Fever (for children)." Yet, such a label has been held by the Commissioner of Internal Revenue to be within the scope of the language of section 600 h.

The following labels would all seem to be within the ruling of the Commissioner of Internal Revenue as to therapeutic indications.

Conjunctivitis.—R acid boracic C. P., 2 grs. Zinc sulpho carbolate, $\frac{1}{4}$ gr.

Cholera infantum.—Zinc sulphocarbolate, 1-20 gr.; salol, 1-10 gr.; bismuth, subnitrate, 1-2 gr.; calomel, 1-60 gr.; pepsin, pure, 1-4 gr.

Cold laxative. Revised.—Each tablet contains acetanilid, 2 grs.; hyoscyamus, 1-4 gr.; ipecac, 1-10 gr.; atropine sulphate, 1-600 gr.; strychnine sulphate, 1-150 gr.; podophyllin, 1-10 gr.; elchoniidia sulphate, 1 gr.

Neuralgic headache.—Acetanilid, 1 gr.; morphine sulph., 1-50 gr.; sodium brom., 5 grs.; caffeine alkaloid, 1-4 gr.; hyoscyamus, 1-2 gr.

Tonic.—(For children.) Calcium phos., 1-10 gr. Iron phosphate, 1-10 gr. One to two before meals, or four to six times daily.

Rheumatic.—Resin guaiac, 3 grs.; fluid ext. poke root, 1 gr.; potass iodide, 2 grs.; colchicine, 1-100 gr.; digitalin, 1-100 gr.

Coryza compound, No. 4.—Dr. Kenyon. Revised. Each tablet contains: Camphor, 1-2 gr.; hyoscyamus, 1-30 gr.; quinine sulph., 1-2 gr.; atropine sulphate, 1-2000 gr.

Grip preferred.—Each tablet contains acetanilid 1-2 gr.; elchoniidia sulphate 1-12 grs.; strontium salicylate 1-2 gr.; tr. aconite 1900, 13-4 min.; capsicum, 1-60 gr.; ext. cascara 1 gr. Dose: 1 tablet every three hours, 2 at bedtime.

Elixir—Strontium Bromide Comp.—Revised. Constituents: Each fluid ounce contains alcohol about 5 per cent and 60 grs. of the combined bromides of potassium, sodium, ammonium, strontium, calcium, and lithium. Indications: Migraine, epilepsy, uterine congestion, acute mania, alcoholism, etc.

Dose: One to two teaspoonfuls in water 3 times a day.

Fever.—(For children.) Tinct. aconite, 1-10 m.; tinct. belladonna, 1-20 m.; tinct. bryonia, 1-20 m.; chocolate, q. s. (Strength U. S. P. 1890.)

Fluid Extract of Cascara Sagrada.—(Fluidextractum cascarae sagradae U. S. P. L. X). Contains alcohol 23 per cent. Made from the dried bark of the trunk and branches of *Rhamnus purshiana*, properly seasoned. Average dose—metric, 1 ml; apothecaries, 15 minims. Properties—An excellent laxative. Particularly indicated in habitual constipation.

EFFECT OF THE TWO OBJECTIONABLE PHRASES.

The 2 per cent tax substantially on gross sales of general medicinal products, exclusive of proprietaries, under the existing statute is oppressive to the manufacturers. A 10 per cent tax on such products can not be absorbed; and, if the tax is to be paid, the manufacturer must add the tax to his price list. This would transfer the burden either to the practicing physician or to the sick, on neither of whom such a tax should be allowed to fall. It is incredible that the Congress ever meant or means now to impose any additional and undue burden of taxation upon those suffering from illness and infirmity or upon the physicians who attempt to alleviate such suffering. Such a 10 per cent tax on gross sales, moreover, ought not to be passed on to the ultimate consumer. The doctors who dispense the ordinary remedies in the sick room ordinarily include the medicine in their regular fees and make no extra charge for it. They certainly ought not to be subjected to the tax and must protect themselves by additional charges.

A TAX ON GENERAL MEDICINAL PRODUCTS DEFEATS ITSELF.

Under the present statute, as interpreted by the rulings of the Commissioner of Internal Revenue, general medicinal products are subjected to the tax, if uttered under a general business trade-mark or under a label bearing any therapeutic indications. In order, therefore, to take general medicinal products out from under the operation of section 600 h, a pharmaceutical manufacturer must abandon the use of his trade name or symbol used as a general business trade-mark and must cease to publish any therapeutic indications on his labels. The alternative thus presented to the pharmaceutical manufacturer is not only unjust to them but is full of peril for the public. General business trade-marks—really trade names—are important to the commercial world and should in every way be encouraged. Therapeutic indications are essential for the public safety and the convenience of doctors and nurses. Proper marks upon containers of medicinal agents are a necessary protection against error and misuse. The ordinary dictates of prudence and propriety call for such marks on a medicinal product as will identify in the shortest possible time the origin of the product, the name of the manufacturer and the therapeutic use of the product indicated by professional and scientific experience. The loss of either of these safeguards would be a matter of grave public concern and a matter of peril to the public health.

The Commissioner of Internal Revenue may be right in his rulings. If he is right the tax defeats itself. General medicinal products ought not to bear a 10 per cent tax. If the rulings of the Commissioner of Internal Revenue are correct the only way out of the difficulty under a statute containing the two objectionable and unnecessary phrases referred to above is to deprive the medical world, the commercial world and the general public of the manifest advantages derived from the use of general business trade-marks or symbols used as trade names and of the protection assured by setting out therapeutic indications on medicinal labels.

OBJECTIONAL PHRASES TO BE STRICKEN OUT.

It is therefore submitted that the words "or trade-mark" and the later words, "or as remedies or specifics for any disease, diseases, or affection whatever affecting the human or animal body" should be stricken from section 600 h or from any proposed revision thereof.

SUMMARY.

It is therefore submitted—

First. That the Congress intended to tax under section 600 h. only proprietary medicinal articles or preparations.

Second. That the language of section 600 h, taken as a whole, necessarily negatives any intent of the Congress to tax general medicinal products.

Third. The words, "or trade-mark" are meant to refer only to special trade-marks asserting some claim of proprietary right.

Fourth. That the words, "or trade-mark" add no new class and extend no previously mentioned class of proprietary medicinal articles or preparations, and are unnecessary unless the Congress intends to tax general medicinal products.

Fifth. That the words, "or as remedies or specifics," etc., are meant to refer only to special remedies or specifics in which some claim or proprietary right is made.

Sixth. That the words, "or as remedies or specifics, etc." are a survival of earlier revenue laws and are now obsolete in view of later legislation.

Seventh. That the words, "or trade-mark" as interpreted by the Commissioner of Internal Revenue tend to embarrass, diminish, and perhaps to destroy the use of general business trade-marks as trade names or symbols.

Eighth. That the words, "or as remedies or specifics" tend toward a discontinuance of the valuable practice of printing therapeutic indications on medicinal labels.

Ninth. That the use of general business trade-marks is of great value to the commercial world and to the public, and should not be interrupted or disturbed.

Tenth. That the use of therapeutics indications on medicinal labels is a safeguard for the public health, and of great importance to the medical profession.

Eleventh. That a tax of 10 per cent on general medicinal products can not be properly absorbed.

Twelfth. That the two objectionable phrases if applicable only to proprietary medicinal articles or preparations are unnecessary and should be stricken from the statute.

Thirteenth. That the two objectionable phrases, if applicable to general medicinal products, as the Commissioner of Internal Revenue has ruled, fail to express the will of the Congress, and should be stricken from the statute.

Fourteenth. That the rulings of the Commissioner of Internal Revenue, whether right or wrong, merely serve to emphasize the confusion resulting from the statute and point out the necessity of having the will of Congress expressed in such clear language that it can not be misunderstood either by the Commissioner of Internal Revenue or by declarants submitting themselves for taxation.

Respectfully submitted.

AMERICAN ASSOCIATION OF PHARMACEUTICAL CHEMISTS.

NEW ENGLAND DRUG MANUFACTURERS' ASSOCIATION.

ATHERTON N. HUNT,

84 State Street, Boston, of Counsel.

The CHAIRMAN. Is there any other representative to be heard now? We will hear one other gentleman on this same point, if he desires to speak, but only one other. Is there any other?

Senator SMOOT. Is there not some one here on the proprietary medicine subject?

The CHAIRMAN. Yes, there are several on this list that represent the Association of Retail Druggists. Is Mr. Brokmeyer here?

Mr. MINICH. I represent the proprietary medicine interests, but the interest I represent is an entirely different interest from that represented by the last speaker.

The CHAIRMAN. We will then hear Mr. Alfred Lucking. State to the stenographer what subject you wish to discuss.

STATEMENT OF MR. ALFRED LUCKING, OF DETROIT, MICH.

Mr. LUCKING. The taxation of dividends; 5 to 10 minutes.

The CHAIRMAN. We will give you 10, Mr. Lucking, and ask you to conform yourself to that time, if you please.

Mr. LUCKING. I will do it. This statement is more to call your attention to a couple of concrete illustrations of the injustice, as we conceive it, of a certain proposed change in the taxation of dividends

under this proposed act from the existing law on the subject rather than to make a general argument. In the first place, I will call your attention to the report of the committee of the House. It will, I think, state the whole question in a nutshell. Then I will give you the concrete examples.

Senator McCUMBER. To what page of the report do you refer?

Mr. LUCKING. This is report No. 767, Sixty-fifth Congress, second session, "Revenue bill of 1918" and "Report." I refer to page 3, under the head of "Definitions." I will read about 20 lines, commencing at the last paragraph on page 3 [reading]:

The dividend provision makes any distribution made by a corporation out of its earnings or profits accrued since February 28, 1913, and payable to its shareholders or members, whether in cash or in other property or in stock of the corporation, subject to tax in the hands of the shareholder, the same as under the present law. It also provides that any distribution made in 1918 or subsequent years shall be deemed to have been made from earnings or profits accrued since February 28, 1913. The present law provides that dividends distributed to the stockholder shall be taxable to the individual at the income-tax rates in effect in the year in which the dividend is received, unless the corporation distributes more than its earnings for the taxable year, in which case the additional amounts so distributed are taxable in the hands of the individual at the rates in effect during the year in which the corporation earned the same. Under the proposed bill all distribution of earnings accrued since February 28, 1913, will be taxable in the hands of the stockholder according to the rates in effect during the year in which the dividend is received.

I think the chairman of the Ways and Means Committee in drawing that stated, with substantial accuracy, the present law as interpreted by the department, but not its exact terms, which might have been susceptible of a different interpretation. The exact language of the act of 1917 is contained on pages 102-103 of the pamphlet "Revenue Laws," and with your permission I will take one minute to read that. [Reading:]

SEC. 31. (a) That the term "dividends" as used in this title shall be held to mean any distribution made or ordered to be made by a corporation, joint-stock company, association, or insurance company, out of its earnings or profits accrued since March 1, 1913, and payable to the shareholders, whether in cash or in stock of the corporation, joint-stock company, association, or insurance company, which stock dividend shall be considered income, to the amount of the earnings or profits so distributed.

(b) Any distribution made to the shareholders or members of a corporation, joint-stock company, association, or insurance company in the year 1917 or subsequent tax years shall be deemed to have been made from the most recently accumulated undivided profits or surplus, and shall constitute a part of the annual income of the distributee for the year in which received, and shall be taxed to the distributee at the rates prescribed by law for the years in which such profits or surplus were accumulated by the corporation.

Now, I want to give you a concrete example of the injustice of the proposed change. The Canadian Bridge Co. is a corporation under the laws of the Dominion, organized by and its stock owned entirely by citizens of Detroit, Mich. I do not remember the date of its organization, but in 1911 it took the contract to build the Quebec bridge, the longest and largest bridge in the world, and they have been building it ever since. You will all remember that the middle span fell. That disaster cost them \$800,000. Practically their entire capital has been invested in that enterprise for the last seven and a half years. It will be eight years by the time the profit, and the only profit, will ever come to them. They are nearing the end now, the bridge will soon be accepted, and all of their net earnings will come to them early in 1919.

Those profits they would like to distribute if they can. It is a Canadian corporation; it is not a United States corporation, but it is owned by our own citizens, and if permitted to distribute they will distribute largely these profits which come, and which are earned, all in a lump. On account of the investment being so hazardous during the whole period they never have been able to distribute any profits up to this time, and now to have the earnings of eight years taxed at the extraordinarily high rate of the new bill it would seem would be a very great injustice to the proprietors who have worked all these years at so great a risk.

Senator SMITH. You say the earnings of eight years would be taxed as the earnings of one year?

Mr. LUCKING. Yes; and at the rates in effect this year, which are higher than the rates in effect a year ago or the year before, and perhaps higher than they will be in one or two years more. It just happens to come at this juncture, when it would take from most of the principal shareholders one-half of their earnings for eight years.

The CHAIRMAN. I understood you to say, too, that you have not in any of these previous years received any profits?

Mr. LUCKING. None from the Quebec bridge operation. They have also done some miscellaneous bridge work, and have earned about 3 per cent during that time—received about 3 per cent—upon the value of their stock. That is my information.

The CHAIRMAN. You will get all your earnings in the final payment?

Mr. LUCKING. Yes; all the profits.

The CHAIRMAN. You have not had these earnings in previous years to be distributed?

Mr. LUCKING. No, sir. We could not have distributed them, because we did not have them.

Senator SMOOT. The same thing applies to railroad and other contractors.

Senator McCUMBER. It applies to any business that has dividends after years of work and preparation. How would you remedy it?

Mr. LUCKING. The existing law is a pretty fair law, and is, I think, practical. It caused some little trouble, I know, in some other cases that I had, in the administration, but a just and satisfactory administration was reached. You tax all that the corporation has earned this year—whatever portion of the dividends is earned this year—tax it at the rate of this year, what it earned last year at the rate of last year, and what it earned the year before at the rate of the year before. It all comes in in a lump to the Government, and it is fair and just. This particular case of the bridge company was not brought to the attention of the committee of the House.

Senator JONES. As a matter of bookkeeping, did your company estimate any profit during these previous years upon that contract in proportion to the amount of work performed, or any other basis?

Mr. LUCKING. I am not able to answer you, but I will be glad to file an answer. No member of my company is here, and I do not know personally. I will have to inquire. I will have that question written out for me and an answer will be filed.

Senator SMOOT. I suppose the estimate was made by those who paid for the bridge, and that was based upon the estimated amount of work on the bridge?

Mr. LUCKING. Yes; and all of their capital was at hazard that they would complete this undertaking.

Senator SMOOT. Yes; of course.

Mr. LUCKING. And they lost \$800,000 on the falling of that span.

Senator JONES. Senator Smoot suggests that this involves a principle that is applicable to many transactions.

Mr. LUCKING. Yes.

Senator JONES. You take a town-site corporation, for instance: It buys land and begins selling land at a profit, but the transaction will not be closed for several years. Now, under the present ruling of the Treasury Department, when a lot is sold the proportionate profit is estimated and is considered as income, as the work progresses.

Mr. LUCKING. Yes.

Senator JONES. And the query which rose in my mind was whether your company should not have estimated from year to year the amount of profit and paid tax on it.

Mr. LUCKING. It has distributed no dividends. You see, that is a Canadian corporation. Anyway, in this particular instance, it distributed no dividends out of the Quebec Bridge earnings, and could not do so; and therefore the gentlemen whom I represent received nothing in the way of dividends or distribution, so that they could not pay any income tax upon it.

Senator JONES. Ought not the Government in such cases as that to at least get the normal tax as the work progressed?

Mr. LUCKING. Yes.

Senator THOMAS. That is what you want now—for the Government to go back and collect that?

Mr. LUCKING. Certainly, Senator.

Senator THOMAS. There might be no profit at all.

Mr. LUCKING. If the bridge had had a second fall, there probably would not have been any profit at all, and all their capital was at hazard.

Senator JONES. It amounts to this, that you have been keeping in a reserve fund, free from all taxation, what you have estimated to meet a contingent liability in the event the bridge should fall or something else might happen, so that you have chosen to allow your profits to accumulate as a reserve fund and insurance fund, we will say, until the completion of the transaction. Now, that is not permitted in a great many laws, in business, and the question arose in my mind whether it should have been permitted in your case or not: whether you are not delinquent now for at least a normal income tax.

Mr. LUCKING. I think not, Senator, because even if this had been a domestic corporation, there would not have been any income tax upon the individual until the corporation declared a dividend, and we had an opportunity to receive something and pay on it.

Senator JONES. But the corporation itself is liable for a tax.

Mr. LUCKING. Yes; of course, the corporation itself pays.

Senator JONES. But in this case—

Mr. LUCKING. Not in this case, because it is a foreign corporation, and it did this work in Canada in that case.

Now, I have one other concrete example. I have exceeded my 10 minutes, and will quickly finish, but I think the time has been exceeded partially on account of the questions. Just one other example. There is a smaller corporation in Detroit known as Nelson.

Baker & Co., a pharmaceutical house, which is not as large as Parke, Davis & Co., but is doing the same line of business. For a number of years they have been each year laying aside a small sum to surplus, and, having a capital of \$400,000, they accumulated something over \$100,000 surplus in a period running over—I do not remember how many years—from five to eight or nine years, laying aside a small amount each year, and they had over \$100,000 at the beginning of this year, and on about the 1st of March they declared a stock dividend of 25 per cent, which is \$100,000.

Senator SMOOT. The first of this year?

Mr. LUCKING. Yes, the first of this year, out of earnings of last year and the years before. That company was paying its taxes regularly, right along, of course, and its stockholders were paying their taxes upon their dividends of 6 per cent which have been drawn regularly for quite a number of years.

Under the proposed bill that will be taxed; that stock dividend, which is of course a mere matter of bookkeeping or at least a paper evidence of the interest of the several stockholders, will be taxed at the rate, for this year, not because they received money but because they received a piece of paper showing that they have 25 per cent more stock.

It seems to us that that is unjust, not only to tax it this year at the rate of this year when the surplus was earned the year before and the year before that and the year before that, in small amounts, but it is unjust entirely because it is not money received; and if this proposed law had been in existence of course in the exercise of wise administration they would not have declared a stock dividend at all.

Senator THOMAS. Then do you think that if earnings are distributed in anything but money they ought not to be taxed?

Mr. LUCKING. I would not want to take quite so broad a position as that, but in this particular case to which I am calling your attention, it seems to me it is not just. Now, they face the position under the existing law that they would have to pay the tax upon it according to the rates when it was earned, in 1917 and 1916 and 1915, and they are perfectly willing to do it; but it seems unjust to tax it, *ex post facto*, now, by a new law making it a very much higher rate than when they committed the act.

I will file a statement of facts about the subject inquired about.

Senator JONES. Yes.

(The following statement was subsequently submitted by Mr. Lucking and is here printed in full, as follows:)

The bridge company having the contract for the bridge (The Canadian Bridge Co. is a subsidiary having a one-half interest in the entire contract and a one-half liability) made a return each year to the Canadian Government of its business, under the business profit tax act, giving its estimated profit for the preceding year, upon the assumption that the total profit was earned at a uniform rate per year during the continuance of the contract. The company paid its tax each year to the Government of Canada, based on these estimated figures, with the understanding that an adjustment would be made when the contract was completed and the final figures could be obtained by which the company would make up to the Government any underpayments of previous years or receive a credit for any overpayments. The estimated figures were made by the company and audited and approved by representatives of the Government. It was understood between the company and the Government that the final total profit should be figured as having been earned at a uniform rate per year during the continuance of the contract and the tax for each year be figured at the rate applying for the year.

The CHAIRMAN. The committee will next hear from Mr. Minich. Mr. Minich, how much time do you want?

STATEMENT OF MR. VERNE E. MINICH.

Mr. MINICH. I requested a half an hour when the appointment was made for me.

The CHAIRMAN. What branch of the bill are you going to take up?

Mr. MINICH. I am going to discuss the matter of allowances, with special reference to patented articles, where the thing which is taxable here is largely the fruit of the efforts of previous years.

The CHAIRMAN. Do you think that will take a half an hour?

Mr. MINICH. I thought perhaps it would, to present it properly.

The CHAIRMAN. Is there any other gentleman here who wishes to be heard on this?

Mr. MINICH. No, sir.

The CHAIRMAN. What is the wish of the committee about that? Will you allow half an hour?

Senator TOWNSEND. Let him go on—let us see how interesting he is.

Senator JONES of New Mexico. The question he raises is one which others doubtless will want to discuss.

The CHAIRMAN. We have ten men on the list to-day. If you can finish in twenty minutes you will confer a favor upon the committee.

Senator DILLINGHAM. Have you a brief?

Mr. MINICH. I have prepared this paper. I will certainly make an effort to finish in the shortest possible time.

The CHAIRMAN. We will be obliged to you, because we do not want to hear any arguments; we simply want to hear a statement of a man's position and hear his reasons.

Mr. MINICH. Mr. Chairman, I could not make a speech if my life depended upon it. I have prepared here a clause for relief which I would like to place in the hands of the members of the committee, if I may, before I start.

Senator ROBINSON. You want it to go in the record of course?

Mr. MINICH. I do.

In House Bill No. 12863, entitled "A Bill to Provide Revenue and For Other Purposes," insert on page 40 between lines 14 and 15 the following additional matter, to wit [reading:]

(14) In the case of business done under an unexpired patent or patents where the taxable income largely represents the fruits of activities antedating the taxable year an allowance equal to the difference between the net income from the business done under such unexpired patent or patents for the taxable year and the total net income from the business done under such unexpired patent or patents since issued, including the taxable year, divided by the number of years since such patent or patents were issued.

Mr. McCUMBER. This is a proposed amendment, is it?

Mr. MINICH. It is a proposed amendment for insertion on page 36, under the head "Deductions allowed," lines 2 and 3, section 234, of the language I have suggested.

I will use this as an example to illustrate the operation of the law as proposed in this House bill 12863, as printed—the effect it would have in my own particular case. We have a machine which is used for the preparation—that is, our chief device—of moulding sand in

foundries. In making preparations for moulding in foundries molding sand is used, and it necessary to moisten and mix that sand, which has always in the past been done with shovels, very laborious work, and at night the labor is performed and the plans prepared for making the castings the following day.

This machine performs the labor much more effectively, and it saves a vast amount of labor; but when the machine was invented and placed on the market it was a new art. Foundrymen are now very much more progressive than they were 10 years ago, and they are looking for labor-saving devices, but at that time they were not, and the way that had been good enough for their father and their grandfather was good enough for them. As the result, the introduction of a machine of this kind was a very difficult matter, and the field was rather limited in that the machine could be applied only to foundries making a specialty of doing a certain class of work where the foundry layout and the size of the foundry would make its introduction applicable.

Reviewing the entire situation we decided that the only practical way of getting the machine on the market profitably and getting a return for our investment and the effort we realized it would be necessary to make to introduce the machine would be to place it on a royalty basis, and it was largely placed on that basis. I personally started the business early in 1908. Then, June 1, 1910, my personal capital being exhausted, I organize a close corporation of \$175,000, distributed \$75,000 in preferred stock and \$100,000 in common stock. This represented the money which the company, as then organized, paid for the patents.

The device was owned by a small concern which was nearing bankruptcy when I personally took hold of it and marketed the device for a couple of years until my capital became exhausted, and showed what there was in the device to the people that owned it then, to the extent that it was necessary, in order to procure control of it—I was then operating under a contract with the owners, during the first two years—for us to pay them \$175,000, and also to assume about \$9,000 worth of their indebtedness to acquire this. Now, we operated up until about 1916, under this patent—or, there were several patents—and for the period I had spent, 1908 to 1910, and the balance of the time that the corporation had spent, the net profit we realized was \$4,778.54 for all those years of time. We had had our machine manufactured under contract outside, not having sufficient capital to start a plant of our own, but in 1915 we did finally start a plant of our own. We were getting our machine pretty well perfected then and we were beginning to get a good many royalty contracts that were on an earning basis, and the tide commenced to turn.

I want to make the point that while we are making a return from our years of effort that would repay us for the nearly ten years that we spent—at least eight years, it was—in getting the thing on its feet, we did not get anything for the eight years, and the returns we are now getting very largely are the result of efforts we made before war was declared, the result of contracts that we had actually closed, and are, in fact, deferred profits that we are now securing.

A great majority of the contracts that we had closed before war was declared on a royalty basis are to-day in operation, and as it

happens the machines are being used by foundries that are making anywhere from 30 to 100 per cent of their product for the Army and Navy in the prosecution of this war.

I do want to make it clear, however, that ours is not a war product and that our growth has only been in proportion, as I can support by figures, to the growth that we enjoyed before war was declared; but it does so happen that the tool is now proving of tremendous value to the foundrymen who are turning out the basic materials out of which machine tools and ships and farm implements, and all the other important requisites of war, are being made, and those tools are rendering a valuable service.

The CHAIRMAN. Is your objection to the income tax on the earnings of the corporation?

Mr. MINICH. Not at all. We have no objection at all to the income tax.

The CHAIRMAN. To what tax are you objecting?

Mr. MINICH. We are objecting to the excess profits tax, or to the so-called war tax, whichever, or both of which, may be enacted in this law. We are objecting to that only to the extent that we conceive it takes inequitably as against years of effort that we spent in establishing in the market and improving a valuable device, which effort was spent under the belief that we had protection from the United States Government in the form of a patent. Patents are granted, as we understand it, by this Government to protect the inventor and the manufacturer of some article for a period of time that will enable such manufacturer to obtain a return for the risk and years of effort that he has taken and made in establishing a market for the device, and unless some form of protection was granted to such inventions it is perfectly obvious that large sums of capital and years of time would not be invested in inventing, perfecting, developing, and creating a market for such devices; and our progress would be very much slower unless some form of protection was granted, by patent or otherwise.

Senator JONES of Arizona. Is your case any different in principle from that of the mining prospector who discovers a prospect, or something which he thinks is liable to develop into a mine, and who spends several years in prospecting that, and finally runs a tunnel and strikes a paying body of ore that is very rich; is your case any different in principle from that?

Mr. MINICH. Yes; I should say it is decidedly different. This law, as I understand it, makes some provision for depletion of that mine, and he is going to enjoy the income of that mine as long as there is ore there. We are going to enjoy protection under our patent until 1923, during which time this law will probably be operative, during which period of time we will have paid the bulk of our returns under the patent out in the form of taxes, and at the end of which time every foundry manufacturer who has another line of machinery on the market and established, conceiving that we have made a tremendous venture out of this, or at least recognizing that it is a very valuable piece of equipment, prepares to manufacture and bring it out and put it on the market as soon as our patents have expired, and he can market it at a very low profit comparatively and deprive us in that way of an opportunity to get any returns for years of effort that we have made in establishing this market.

Senator JONES of Arizona. Then you simply want the exemption to take into consideration the life of the patent as a depletion charge?

Mr. MINICH. Yes; I think, if I understand your question correctly, Senator. The substance of this amendment which we have proposed is as follows. It being very brief, perhaps I may be permitted to read it. It is as follows [reading:]

In the case of business done under an expired patent or patents where the taxable income largely represents the fruits of activities antedating the taxable year an allowance equal to the difference between the net income from the business done under such unexpired patent or patents for the taxable year and the total net income from the business done under such unexpired patent or patents since issued, including the taxable year, divided by the number of years since such patent or patents were issued.

In other words, we are simply seeking the opportunity to pay whatever tax may be levied upon the average returns that we enjoy from this patent.

Senator JONES of Arizona. How different is that from the case of the prospector to which I referred a while ago, who puts in ten years discovering a body of ore, and when he discovers it, he discovers enough to warrant operation for ten years longer; but under your plan, you would have the profit distributed over a period of twenty years.

Mr. MINICH. Seventeen years, Senator; pardon me.

Senator JONES of Arizona. Well, seventeen years in the case of the patent, and twenty years in the case of the mine, which I mentioned. Is not that just the same thing?

Mr. MINICH. As I understand it, he is permitted to deduct for the depletion of his mine, assuming it is going to be exhausted in ten years, each year, 10 per cent; so that each year he pays on the average income he gets from his mine.

Senator SMOOT. But in the case of the mine, you have not anything left at the end of the time, while in your case you have the right of manufacturing that machine as long as you want to.

Mr. MINICH. Quite so; but all of our royalty income, all of the income upon the basis upon which we have done business, is extinguished. We must discontinue; when our patent expires, we can no longer secure a royalty on this machine.

Senator SMOOT. Take any class of business; many of them run for years without any profit at all, but in your case you are protected by your patent for seventeen years.

Mr. MINICH. Precisely, and we worked on it for eight years.

Senator SMOOT. What is the difference between you working eight years and a merchant working eight years to get his business on a paying basis?

Mr. MINICH. I should have explained that four years of our patent had expired when we acquired the right to it, leaving us only thirteen years.

Senator SMOOT. Yes.

Mr. MINICH. The difference is this, that the merchant is building up his business upon an ordinary competitive basis, but it is built up in competition all the time. All of the profits he obtains under that he is in position to enjoy equally at the end of the period. We are not.

Senator ROBINSON. You enjoy all the benefits during the period. You have in effect a monopoly during the life of the patent.

Mr. MINICH. Precisely so.

Senator ROBINSON. And at the end of the patent period you go upon the basis that the merchant is now occupying.

Senator SMOOT. Yes; and that you do not want to do.

Mr. MINICH. What I am pointing out is this, that presumably the United States Government is giving us some form of protection in the form of a patent, which protection by the operation of this law we are deprived of.

Senator ROBINSON. But in granting your patent it did not give you an immunity from taxation. That is the fundamental error, if I may say so, in your position.

Senator GERRY. What you would really like to have to-day is to have your patent lengthened?

Senator JONES of Arizona. You want the period of your patent to begin when you begin making a profit out of the business.

Mr. MINICH. No, I am not seeking any of those things. I am simply seeking the privilege of paying a tax based upon the patent, based upon the average return that we realize from this patent.

Senator ROBINSON. But you did not realize those returns during former years?

Mr. MINICH. How is that?

Senator ROBINSON. You did not realize substantial returns during the former years?

Mr. MINICH. I have explained these things. You take a standard article of merchandise and start in to manufacture; that device is known to the trade; it is a device that the trade is using. You do not need to go to the great expense of developing that device mechanically, to the great expense of creating a trade for something that is not known, the value of which is not recognized or known. You go into the market and place this device upon an ordinary competitive basis; it is something that is already known and for which a market is already established. It is simply a question of salesmanship, of showing him that your device, for something he wants, is going to do better than his device. You are in a vastly better position; I submit that no one would go to the trouble of inventing devices—I mean something that covers a new art—inventing such devices—

Senator JONES of Arizona. I think you are touching upon a phase which has caused some of us, at least, a great deal of concern, but I cannot distinguish between your point where a patent is involved, and other lines of business which meet with the same difficulty.

Mr. MINICH. My proposition is this, that patents, the development or improvement of devices covering a new art, will be greatly disturbed and there will be very much less in the way of invention during the period of the war on devices which relate to a new art, which it is well recognized in the commercial world requires a vast deal of time and expenditure of effort, and so on, before there is any hope of return, if some protection cannot be obtained; so that the fruits of the effort put upon that patent can be enjoyed upon a basis somewhat equal to the marketing of a standard commercial device by the commercial manufacturer.

Senator THOMAS. Substantially, then, you think that the profit which this will reach as war profits should not be considered

as a war profit because it is based upon previous years of very earnest effort?

Senator SMOOT. That is it.

Mr. MINICH. Partly that, and partly because it so happens that coincident with the passage of this bill which takes the largest percentage of our returns, we are just beginning to get returns.

Senator SMOOT. I know a mine in my own State that has been working now for nearly 20 years. About six months ago, or at the beginning of this year, they struck a very rich body of ore. They have made a million dollars out of that body of ore. Perhaps they will never make a hundred thousand dollars out of it again as long as they live. Under this bill they are taxed, and it will take at least eight hundred thousand dollars out of that million dollars.

Senator THOMAS. That is not war profits, at all.

Senator SMOOT. Mind you, now, if they did what you want done they would divide that by 20 years, because of the fact that they had been spending money all of that time and never struck ore sufficient to pay the running expenses of the mine. The only difference between this mine and your business is this, that they have taken the ore out and nobody but God Almighty could put it back. It will never be found again. They paid out their capital. You are not doing that, and you are protected for so many years, and then you can meet them on the other basis and make the same machine in competition with anyone else, and you stand a chance there of making your profits there just the same as you would if you were in competition with business men in any line of endeavor.

Senator McCUMBER. Both cases are unjust; there is no question about that.

Senator SMOOT. Both cases are unjust.

Senator McCUMBER. The only question is whether we can avoid it.

Senator TOWNSEND. There is another feature of that case, if I understood your illustration correctly, that I would like you to consider. You want this profit which you receive this year distributed over the period of years during which you have been operating. You also stated a moment ago that there had been additions made to that patent from time to time.

Mr. MINICH. Yes.

Senator TOWNSEND. You have been making additions?

Mr. MINICH. Yes.

Senator TOWNSEND. Maybe your patent was not worth much of anything to begin with, but you have got something recent, within the last year, maybe, that has made your patent profitable. Do you think you would have any right to ask the Government to go over those unprofitable years and distribute these earnings now, as of the period when it was not profitable?

Mr. MINICH. I do not think so, if that was the case. It is not the case. The patent which we are really relying upon for protection was issued in June, 1906, and will expire in 1923, and then we will be without protection after that date.

Senator TOWNSEND. But you said a moment ago that you have been making additions to it. I take it that something was not right about it.

Mr. MINICH. We have been making mechanical changes in our device. Our first model, to illustrate the point, was type A, and that

was made under our patent. Our next model was type B, and there followed types C, D, E, F and G, and now again we have double A, all of those models being made and protected under the original patent only. That was simply mechanical development work, not patent work.

Senator SMOOT. What will your income be for the year 1918?

Mr. MINICH. As near as I can judge, around \$90,000.

Senator SMOOT. With an investment of \$175,000?

Mr. MINICH. We have more investment than that now, I should say. Perhaps the investment will be \$200,000.

The CHAIRMAN. When did you commence to make this profit?

Mr. MINICH. We commenced to make a profit in about 1916.

The CHAIRMAN. That was after the war began?

Mr. MINICH. Yes, sir.

The CHAIRMAN. You had made no profit up to that time?

Mr. MINICH. We had made up to that time \$4,778.54 net profit.

The CHAIRMAN. That was in 10 years?

Mr. MINICH. No; that was in eight years.

The CHAIRMAN. You said a little while ago that since the war broke out a great many additional uses have been found for this machine?

Mr. MINICH. No; what I said was this, pardon me, Mr. Chairman—that it happened that the foundries with whom we had placed these machines before the war under royalty contracts were now turning out their product especially for the United States Government or for those industries which are regarded as essential in the winning of the war.

The CHAIRMAN. Does not that mean that your patent is used in connection with industries that are connected with the winning of the war?

Mr. MINICH. It is being used so, largely, now; but let me explain this point, that those concerns which are now turning out this material, we will take for example the Oliver Chilled Plow Works at South Bend, Ind., an agricultural implement concern, making agricultural implements which are considered very essential in winning the war, in growing crops.

Then there is the Bath-Avery Co. at Louisville, Ky, a similar concern. Then there are still other concerns like the American Blower Co., who make blowers and exhaust pans, and so on. They are making the same material that they were making before the war, and they were using the same machines before the war, to the same extent that they are now.

Senator McCUMBER. The war, because of the fact that it has caused a shortage of labor, and conditions growing out of the war, compelled these people to use your machine and thereby your machine became more valuable and your income larger because of the war?

Mr. MINICH. I can show that our income has only increased in proportion in the same ratio as before war was declared. I simply make the point that the machine is proving of very material value; the fact being that these people who had the machine in service before the war are now using it on products which the Government is now taking. They were using it before the war to the same extent, and I will say that the income from the machines from these same

people was relatively the same as it is now, but it so happens that it has proved of material value in that these materials which they made before the war are now being taken by the Government and are being used by the Government.

Senator SMOOT. In increased quantities?

Mr. MINICH. Yes.

Senator McCUMBER. They are doing a greater business, and therefore you are getting a greater income?

Mr. MINICH. Possibly they are being used in greater quantities. Our income, which is based upon quantities, does not indicate an increase of the output. These concerns with whom we have always done business were the leading concerns, which even under the pre-war period were running at full capacity, and their capacity has not been materially increased. They do make the point, that under present labor conditions they could not maintain the capacity which they did maintain before the war but for the assistance of the machine now gives them.

The CHAIRMAN. Have you a brief?

Mr. MINICH. I have only what I have submitted there in the form of an amendment. I shall be very pleased to submit a brief.

The CHAIRMAN. If you desire to submit a brief you may do that. I think the committee understands your point.

Mr. MINICH. Thank you, gentlemen.

(The brief referred to is here printed in full, as follows:)

SEPTEMBER 16, 1918.

The CHAIRMAN AND MEMBERS,

SENATE FINANCE COMMITTEE,

Washington, D. C.

SIRS: In support of our proposed amendment to H. R. 12863 for insertion on page 40, between lines 14 and 15, attached hereto:

I wish to outline, as an illustration of the hardship and inequality of the operation of existing law and the proposed new law, a brief financial history of our own business.

This business is founded upon a patented invention for the daily preparation of sand for making castings in gray iron, malleable, steel, and aluminum. It was started in 1908 by myself, operating as an individual under exclusive rights which I obtained from the owners of the patent. After exhausting my capital I organized a company on June 1, 1910, which was incorporated for \$175,000, all paid in, in cash. This entire sum was paid to the original owners for the patent and good will.

The work performed by the machine had previously been done by hand. To overcome prejudice against a new method was slow and costly. The early machines were crude and imperfect and had to be scrapped and new types designed. Seven types were designed and completely scrapped after being built and put in service in some numbers and found wanting, before the present type was adopted, in 1916. In this way practically all of the profit of the previous years' efforts was spent in the development of the machine to bring it to a state of practical perfection. Not a dollar of the earned profit, which was put into the mechanical development of the machine, was added to the capital account, but was all charged off to expense. No stockholder other than myself ever drew a dollar of salary, or compensation in any other form, and all of these years, and up to date, I have drawn a salary equal to only 60 per cent of what I was receiving when I resigned my previous position to start this business. The net surplus and undivided profit from May 1, 1908, to June 1, 1916, was only \$4,778.54. The machine was marketed on a royalty basis from the outset. Just as soon as the expense for designing and scrapping machines was stopped by the perfecting of the machine, the income from royalties, which was the result of eight years of cumulative effort, commenced to show a profit. That the larger net income enjoyed thereafter was not due to the war

is shown by the following table giving the gross income from royalty collections, year by year:

1908, June 1-Dec. 31, 7 months	\$892. 16
1909	10, 101. 68
1910	21, 007. 49
1911	32, 178. 62
1912	42, 211. 32
1913	53, 113. 04
1914	57, 083. 13
1915	64, 059. 75
1916	82, 794. 91
1917	122, 657. 32
1918, Jan. 1-Aug. 31, 8 months	100, 485. 28

EXPLANATORY NOTE.—At the middle of 1916 we had unfilled orders on our books which had been accumulating for almost one year while we were changing from the plan of obtaining machines under contract to making them ourselves. This accounts for the slightly disproportionate increase between 1916 and 1917.

From the foregoing figures it will also be evident that a large proportion of the income upon which we are being assessed excess-profits taxes and war-profits taxes is income from royalty contracts closed before the war. It will further be evident that if these machines now out on royalty had been sold and the proceeds added to our capital the lawful deductions would be much greater and the income subject to the present tax would be appreciably less.

Our belief is that in the granting of a patent the Government intends to give a limited monopoly to encourage inventions. Our machine was not merely an improvement upon some device already known and accepted and in demand by the trade. On the contrary, it constituted a completely new art. It is a well-known fact that years of costly effort are always necessary before any device which represents a new art can be made commercially profitable. If, as is true in the present instance, a tax scaling up to 60 per cent or a flat tax of 80 per cent is levied upon the income from a patent upon which years of effort and substantial sums have been unprofitably spent, and which has but few years remaining before it expires in which to earn a compensating income, the effect will be to defeat the obvious original purpose of the Government in granting such protection. This will surely remove all incentive to men to risk their time and money in inventing and perfecting valuable mechanical devices. The case is quite different from that of a standard article of commerce, sold in competition, for the reason that for such articles the demand has already been created, the market exists, and it is only a problem of good salesmanship to promptly secure a profitable sale for such products. But with an unknown invention the demand must be created, which is always a slow and costly process, regardless of the merit and the value of the device.

Also the case differs from that of mines or oil wells in that, even though as much time and money may have been unprofitably spent in finding the oil or uncovering the ore, the owner of the well or mine may use his discretion as to when he will pump out and sell the oil, or mine and dispose of his ore. But with a patented article it is now or never, as, with each passing day, the expiration date draws nearer.

Therefore, we submit our belief that, in the case of such patents, the excess-profits tax and the war-profits tax should be levied upon the average income during the life of the patent, as provided in our proposed amendment, and not upon the income of the few years only during which it makes a profit.

Yours, very truly,

V. E. MINICH,
Vice President and General Manager.

PROPOSED AMENDMENT.

In House Bill No. 12883, entitled "A bill to provide revenue and for other purposes," insert on page 40 between lines 14 and 15 the following additional matter, to wit:

"(14) In the case of business done under an unexpired patent or patents where the taxable income largely represents the fruits of activities antedating the taxable year an allowance equal to the difference between the net income from the business done under such unexpired patent or patents for the taxable

year and the total net income from the business done under such unexpired patent or patents since issued, including the taxable year, divided by the number of years since such patent or patents were issued."

The CHAIRMAN. The next gentleman on this list is Mr. Frank A. Blair, vice president of Foley & Co., Chicago, Ill., manufacturers of proprietary medicines.

Mr. BLAIR. I have also been asked to represent the National Wholesale Druggists' Association, their representative being not able to get here on account of illness.

The CHAIRMAN. How much time do you want?

Mr. BLAIR. Give me 15 minutes and I will try to take less.

The CHAIRMAN. You may take 15 minutes, but be as brief as you possibly can.

STATEMENT OF MR. FRANK A. BLAIR, VICE PRESIDENT OF FOLEY & CO., OF CHICAGO, ILL.

Mr. BLAIR. We simply wish to call to the attention of the committee two or three what seem to us to be injustices to our industry under the present tax, which under the pending bill will be accentuated because of the increased rate. If they are unjust on the present basis, as the basis is increased and there are changes, the injustice becomes greater.

The first thing is the definition of "invested capital." Proprietors or manufacturers of proprietary medicines have their greatest investment—in fact it amounts to 85 per cent of their investment—in good will, formula, trade-mark, brand, and secret process, none of which is recognized under the present definition of "capital." This is all familiar to the committee, and I do not intend to elaborate on it, but file a short brief and simply to call attention to the fact that under the new bill we have not been given any relief.

In administration the Treasury Department appointed an advisory committee before whom we appeared, and that advisory committee did give us at this time a temporary relief—that is, they have, to use their own language, gone as far as they could under the limitations of the act in recognizing our claim. We are not claiming any value for nonearned increment. We are claiming just for money that we have actually invested in the business. It is actual investment, running over a period of years; and it is unfair as between manufacturers in our own business. One manufacturer, for instance, having bought his business outright and having paid for it a definite sum of money, the sum of money which he has paid is usually equivalent to, or somewhere near equivalent to, the amount of money which the man has paid into the business to build it up. A man who sells it does not make anything. He simply cashes in on his expense up to that time.

Senator JONES of New Mexico. Do they not often make a profit?

Mr. BLAIR. Do they not often make a profit?

Senator JONES of New Mexico. Yes.

Mr. BLAIR. I think not. I think often businesses are sold for less than what was put into them, cashing in a large amount on direct sale, but not getting back all that was put in it. These direct sales have usually been made on the basis of five or six years' earnings. A few organizations in the country have been buying businesses which were going businesses, established, going, prosperous companies. They will buy them on this basis; they will put their bookkeepers

and auditors in your plant and they will pay based on the earnings of from five to six years.

Senator JONES of New Mexico. You take a concern that has built up a very valuable trade-mark; it is not willing, ordinarily, if it has been very successful, to sell it simply for the amount of money that has been spent on advertising and making the trade-mark valuable, is it?

Mr. BLAIR. The records would indicate that it has been sold for, frequently, one-third of the amount of money spent in advertising. It is the tradition of the trade that probably two-thirds of the amount is sales expense, and one-third might be justly charged to constructive expense. It has not been our custom, however, to do that, but we have charged all the advertising to sales expense, and we have that judgment, that one-third is chargeable to constructive expense.

Senator JONES of New Mexico. It is not profitable to build up a trade-mark, then, is it?

Mr. BLAIR. We have been taking profits out of it at the same time, of course.

Senator JONES of New Mexico. But yet you say that when you go to sell it you will sell it for about one-third of what it cost?

Mr. BLAIR. No, I said one-third of the advertising expense, Senator.

Senator JONES of New Mexico. Is not that about the same thing?

Mr. BLAIR. No, I said two-thirds are justly chargeable to sales expenses. Some of us use no salesmen. Others use salesmen. Where we use no salesmen, the advertising expense is our only expense.

Senator JONES of New Mexico. You would not consider that as part of the cost, then?

Mr. BLAIR. No; I say approximately one-third of this money which we have spent for advertising has given a real value to our property. The trade-mark is property which has a real value. It passes as a part of an estate. It is admissible in a general assignment for the benefit of creditors, and is in every way recognized by the law as property, except in this definition of invested capital, where it says not. Now, we simply ask that in the rewriting of the revenue bill taxes shall be imposed on an equal basis; that we shall be given the same opportunity as the manufacturers in other lines of business and as competitors between ourselves. I have elaborated somewhat on that in a short brief which I shall file.

The CHAIRMAN. How are you going to ascertain the value of a trade-mark unless it has been sold?

Mr. BLAIR. Under the act of September 8, 1906, if I remember right, a tax is imposed on the capital stock—a Federal capital stock tax. The Treasury Department has collected that. The present bill doubles that tax. It is small. They have collected that and they have ascertained the actual value, based on the earnings, and they have taken into account, they have recognized there, the good will of the trade-mark, the brand, and the secret process, and they have there the machinery for doing so. If our business is overcapitalized—

The CHAIRMAN. You are speaking about the tax on the capital stock, now?

Mr. BLAIR. Yes.

The CHAIRMAN. We allowed there the value on the market of the capital stock.

Mr. BLAIR. Yes; and it is based on that, and the Treasury Department has there the machinery for that purpose.

Now, I have another suggestion. My suggestion would be under section 210 of the old bill, or 327 of the new bill, where the Treasury or the commissioner have the right to compare like or similar businesses. And do not forget that under the bill he is prohibited from considering trade-marks as having a value. He is not allowed to do it, although he is allowed to consider legal inequalities. He is prohibited from considering them, and they have said, "Your relief is in Congress. We have gone as far as we can."

The CHAIRMAN. Your point is that in capitalizing you they should place some fixed value upon a trade-mark?

Mr. BLAIR. Yes.

The CHAIRMAN. Now, the question I asked you was, how will you compute that value? What standard will they fix it by? How do they know what the value of the capital stock is, measured by the trade-mark; and if there is no capital stock to measure it, on what basis would they estimate its value? Of course, if the trade-mark has been sold, then under the bill it can be considered, because it represents an actual outlay; but where the trade-mark has not been sold, would not any estimate that they might make be a mere guess?

Mr. BLAIR. My suggestion, outside of the machinery which the Treasury Department has for that purpose, would be under section 210 or under section 327 comparison with like or similar businesses. If A has a business which has been sold for which he is paid \$1,000,000, A's business may have brought \$200,000 last year; it may be 20 per cent. B, we will say, has a business that has been conducted over a similar number of years, and he made \$200,000, but he has an investment of only \$25,000 or \$30,000. That is all he has invested. It is patent that that does not represent all the money that has been put into it, and yet, by comparison of like or similar businesses, the Commissioner might well arrive at a fair valuation of these businesses.

The CHAIRMAN. Your contention, then, is that if the taxpayer owns a trade-mark which he thinks constitutes a valuable part of his assets, that fact ought to entitle him to the benefit of the like business clause of the bill?

Mr. BLAIR. I do. Do not overlook the fact that it is not the trade-mark alone; that the trade-mark without the good will is not worth anything. No matter how valuable a suggestion the trade-mark may be, if it is only worth \$50 or \$200, it is just a suggestion, and you have got to put the money behind it and advertise it and create the good will before it is worth anything. It is trade-mark and good will.

I think I will not say anything more on the score of proprietary manufactures. I think you are all familiar with that.

But we have a second and still a third place in which we are heavily taxed. Alcohol is used in medicines. It is practically impossible to secure the strength of the drug without alcohol. It is also used as a preservative, and it is used for triturating and in granulating. We must use alcohol. Formerly there was a tax of 90 cents a proof gallon. It became \$1.10. Under the present bill it is \$2.20 a proof gallon. It is proposed to make it \$4.40; \$4.40 a proof gallon becomes \$8.20 a wine gallon on alcohol such as the medicine manufacturers

use; \$8.20 a wine gallon is a higher tax than it is proposed to put on whisky. It is proposed to be taxed \$8 a gallon, and it is less than proof—proof or less.

Now, I took a survey of some of our industries to find out what percentage that would amount to of their gross business. I found in the case of one of the old liniments, which you will find in most of the stables of the country as well as in most of the homes, because it is used for beast as well as for man, they told me that if they had paid the tax on their alcohol consumption of 1917, it would have amounted to 51.7 per cent of their gross sales. Other manufacturers reported from 10 per cent to 35 per cent of their entire sales. The larger percentages were in the cases of manufacturers who had liniments in their lines, and the smallest, 10 per cent, was in the case of a manufacturer who markets nothing in liquid form, but only pills and tablets, and who used it only for granulation and extraction; so that there is a tax imposed there which ranges from 10 up to 52 per cent.

The CHAIRMAN. Would this apply to proprietary medicines only or to all medicines?

Mr. BLAIR. It applies to all medicines.

The CHAIRMAN. This 51.7 per cent you speak of?

Mr. BLAIR. That applied to liniments.

The CHAIRMAN. Liniments have a large percentage of alcohol.

Mr. BLAIR. A very large percentage.

The CHAIRMAN. The fact is that the proprietary medicines have a great deal larger percentage of alcohol than the common medicines?

Mr. BLAIR. No; a much smaller per cent. When you say "common medicines," I take it to mean physicians' prescriptions.

The CHAIRMAN. I mean the medicines that are sold over the counter.

Mr. BLAIR. The medicines that are sold over the counter? They are proprietary medicines.

The CHAIRMAN. They are not proprietary medicines?

Mr. BLAIR. Yes, they are almost all proprietary medicines; and I am addressing myself only to such preparations as may not be sold for beverage purposes. We have not in our list a single article that may be sold for beverage purposes. Do not make the mistake of thinking for a moment that these articles are taxed under the liquor tax, for we are representing only such manufacturers as manufacture such medicines as may not be sold for beverages, which are medicated sufficiently so that they can not be so sold; and that is covered under the pure food and drug act of October, 1916.

There are other liniments besides this to which I have referred in which, in my opinion, the percentage of alcohol would be higher than 51.7. I did not happen to get the information, but I believe that the percentage of alcohol would be even higher than 51.7 per cent of their gross sales.

Senator TOWNSEND. That same thing applies in extracts very largely, does it not?

Mr. BLAIR. Yes; extracts come pretty close to that. We do not have extract manufacturers in our organization.

There is one other feature I would like to mention, there. Denatured alcohol does not pay a tax. I do not believe the alcohol used in the manufacture of medicines has any more right to pay a tax

than denatured alcohol. I do not see why it should. Medicine is for the sick, and why should it be taxed at the rate of \$8.20 a gallon? I do not believe, in the first place, that the members of the Ways and Means Committee realized that they were placing that tax. We must use wine gallons in our computation, because we are required by law to state on our package the percentage in volume of alcohol, so that we always state it in wine gallons.

Senator THOMAS. Did you appear before the Committee on Ways and Means of the House?

Mr. BLAIR. If you noted the hearings, this was put in at the eleventh hour. It was put in at the last minute. I appeared before the other committee on the subject of excess-profits tax, and the definition of "invested capital" and the specific tax, but not on this, because we had no opportunity on this.

The CHAIRMAN. You knew that it was the purpose of that committee to develop this tax all the way through? That was announced in the papers.

Mr. BLAIR. No; but, Senator, if you will remember it—

The CHAIRMAN. You had a differentiation in favor of spirits used in medicine in the last bill, and that differentiation is simply carried forward in this bill.

Mr. BLAIR. But if you will remember, the recommendation of the Treasury Department was this. Under the previous bill we were taxed \$2.20.

The CHAIRMAN. Yes.

Mr. BLAIR. On beverage alcohol the recommendation of the Treasury Department—at least the printed recommendation, which is all I have—was that the tax should be doubled.

The CHAIRMAN. Yes.

Mr. BLAIR. We took that literally and did not make any report regarding nonbeverage, because we thought it excepted; that the recommendation of the Treasury Department in that respect would be followed. Instead of that the tax was doubled.

The CHAIRMAN. While the tax on spirits used in medicine was doubled, the tax on spirits not used in medicines was more than doubled.

Mr. BLAIR. Yes.

The CHAIRMAN. As I say, substantially the same differentiation was carried through.

Mr. BLAIR. We are even at a greater advantage.

The CHAIRMAN. What is that?

Mr. BLAIR. There is even a greater differentiation in this present bill.

The CHAIRMAN. Slightly, yes.

Mr. BLAIR. Yes; but the burden has already become very high. We pay to-day approximately 80 cents a gallon for alcohol on which we are to-day paying \$4.10 tax. Under the proposed bill we are going to pay \$9 for alcohol; that is, we will pay 80 cents for the alcohol and \$8.20 tax.

Now there is still another feature of it.

Senator McCUMBER. I think you can add Sherman's phrase about war there.

Mr. BLAIR. Yes, we can do that very well. You will think so, after I call your attention to the next one.

The CHAIRMAN. Somebody else besides taxpayers finds that out, too.

Mr. BLAIR. Yes; our boys.

Under the present bill a sales tax of 2 per cent is imposed on the manufacturer. Under the proposed bill a tax of 10 per cent will be imposed. I am using the term "10 per cent" because it is for comparative purposes. That means 1 one cent on each 10 cents or fraction thereof. We have asked that this be, instead, 4 per cent, and we are basing our request upon the proposed volume of the bill. We are paying 2. It is proposed to double the bill, and it seems to us that it would be our fair share of the burden in addition to the other thing if we were charged 4, but we suggest that this be made a consumption tax paid by the consumer at the time of purchase from the retailer, by affixing a stamp; and again I am using the term "4 per cent" for comparative purposes. We suggest that it be 1 per cent on each 5 cents or fraction thereof. As the sales are going to-day, it would give approximately five times as much as the manufacturer's 2 per cent tax, and would not be burdensome, particularly.

The CHAIRMAN. Do I understand you to say that you are willing for the tax to be increased if we would relieve the vendor and let it go to the purchaser?

Mr. BLAIR. It will go to the purchaser, no matter where you put it.

The CHAIRMAN. But you want it directly put on the purchaser?

Mr. BLAIR. I want it directly imposed on him.

The CHAIRMAN. You do not want simply the privilege to put it on, but you want the right to put it on?

Mr. BLAIR. I ask the committee to collect in that manner. The consumer will then pay 25 cents for his bottle of medicine and 1 per cent tax.

The CHAIRMAN. The law requires the seller to pay the tax?

Mr. BLAIR. Yes.

The CHAIRMAN. You are willing to have us double the tax if we are willing to require the purchaser to pay it?

Mr. BLAIR. Yes, sir.

Senator THOMAS. That is very humanitarian and philanthropic. [Laughter.]

Mr. BLAIR. Perhaps not so much as you think. Our costs have increased. We will not absorb it, no matter where it is put. We did not absorb the last tax, taking it as a whole, as anybody who is informed about it knows.

Senator JONES of New Mexico. Have you any objection to making that 2 cents instead of 1?

Mr. BLAIR. Well, I think that 1 cent is enough. It collects five times as much as the present tax. But we are only trying to raise twice as much money. The suggestion of the Ways and Means Committee was somewhat higher.

Senator JONES of New Mexico. If a fellow should be sick and wanted a sure remedy, he would not hesitate on paying an additional cent, would he?

Mr. BLAIR. Sometimes the man who is sick and wants the remedy has not the money to pay. We must not ask him to pay too much.

Senator JONES of New Mexico. If he had not the 2 cents he would not have the 1 cent.

Senator THOMAS. This bill practically, in its ultimate consequence, imposes the great bulk of this \$8,000,000,000 upon the consumers of the country?

Mr. BLAIR. Yes; it will be passed there. It must be passed there.

Senator THOMAS. They are the ones that should think of Sherman's celebrated and truthful saying.

The CHAIRMAN. Are there any other questions. Have you anything further?

Mr. BLAIR. No, sir. I will file a statement for the record.

(The statement referred to is here printed in full, as follows:)

STATEMENT BY FRANK A. BLAIR, VICE-PRESIDENT OF FOLEY & CO., CHICAGO, ILL., MANUFACTURERS OF PROPRIETARY MEDICINES, ALSO PRESIDENT OF THE PROPRIETARY ASSOCIATION, A NATIONAL ORGANIZATION OF MANUFACTURERS OF PROPRIETARY MEDICINES.

We appreciate the demands of the country for increased revenue. The pending revenue bill will greatly increase the taxes. We appear only for the purpose of discussing the subject of inequalities in the present system, with the hope that we may aid the committee in arriving at some method of procuring the required revenue in a just and equitable way.

The President in his message pointed out that there are inequalities in the present revenue bill, and necessarily the proposed increase in rates upon the present basis will emphasize such inequalities.

One instance under the present law in which inequalities appear particularly unfair results from the definition of invested capital. Under this definition concerns engaged in similar businesses, having identical amounts of investment, whether such investment represents a purchase or an increased investment of profits, are unequally taxed.

For example a manufacturer began business many years ago. By reason of the excellence of his product, large investment in advertising, careful and conservative management, and faithful attention to his business, he has built up a large and profitable concern.

His competitor, engaged in the same line of business, has acquired his property by direct purchase, paying therefor a sum of money equivalent only to its value and in an amount not in excess of the amount expended by the first individual in the building up of his business. The former is penalized by a tax of 8 per cent upon what is really the actual value of the capital invested in his trade-mark, brand, and good will. This is an unjust, unfair, and inequitable system of taxation.

If, therefore, the basis of determining the point at which taxes upon income are to be imposed is made the actual value of the property rather than an artificial definition of invested capital, like taxes would be assessed upon all engaged in similar business.

We appreciate that if it be the purpose of the Congress to impose a tax upon unearned increment or upon values which have been developed irrespective of the amount of money actually originally invested in an enterprise, it would probably be within the power of Congress to impose such tax, but as we are treating the subject of taxes imposed upon incomes, based upon the percentage of income to investment, the tax should be alike in all instances.

If the income is the same and if the credits or property which produces that income is the same, the tax ought to be the same. If, however, a tax is to be imposed upon values which have been developed then that should be the subject of substantive legislation and all treated alike. But if you are imposing this tax upon incomes then the tax should be fairly and equitably distributed.

Manufacturers of proprietary medicines have expended large sums in advertising to give real value to their property; therefore it can not be said that the value of their property depends upon something unearned. This value is not an unearned increment, but represents actual money invested, although not within the definition of invested capital found in the present revenue law.

The value of a proprietary medicine concern is largely represented by its trade-mark and good will, which usually represents approximately 85 per cent of its total value.

This trade-mark and good will is property which has a real value, which passes by purchase, is transmissible under a general assignment for the benefit of creditors and may be administered as a part of a decedent's estate. Why should it not be considered as well as any other class of property in determining the amount of invested capital?

Under the proposed revenue law not only is this value excluded in determining the deduction but it is in the nature of a penalty imposed upon the manufacturer who is conservatively capitalized and who has built up his business, and places him in an unfair and inequitable position with respect to his competitor, who has purchased the property outright for its value.

We ask that in the rewriting of the revenue bill the taxes shall be imposed upon an equal basis. That in determining the amount of excess profits, which is to be taken by the Government by way of revenue, that all manufacturers shall be treated alike. Reference to the records of the Bureau of Internal Revenue will give you full and complete information as to the amount of our earnings. If for the conduct of the war, it is necessary to take our earnings, take from us as from others and we will have no complaint. We ask only that you shall impose a tax upon us that is imposed upon other industries and that the tax imposed upon our industry shall fall with equal burden upon all engaged in the industry.

In this behalf your attention is called to the fact that the Congress in the revenue law of 1917 realized that the hard and fast rules already laid down were apt to work inequalities and for that reason provided in Section 210 a partial means of relief. The advisory committee appointed to assist the Treasury Department in the administration of the income and excess profits title, so far as they were able, tried to grant relief to the owners of franchises and trade-marks. It was pointed out by them, however, that they had gone as far as they could in the matter and they suggested that the only way in which proper relief could be obtained would be through amendments to the titles by Congress.

It has been stated that it would be extremely difficult to determine the actual value of capital invested. We respectfully suggest that to obtain this basis is not at all difficult. On September 8, 1916, an act of the Congress of the United States was approved, which contained, among other things, a provision for the assessment of a tax based on the fair value of its capital stock and in estimating the value of its capital stock, the surplus and undivided profits should be included. Under the provisions of this Act, the Bureau of Internal Revenue have devised a system of imposing taxes whereby the actual value of the property has been as nearly arrived at as can be. Where the capital stock has been of less value than its face, the corporation has been billed for the real value. Where the corporation has been conservatively capitalized, the corporation has been billed for the actual value irrespective of the outstanding capital issued and in determining this value they have taken into consideration the value of trade-marks and good will. So that the Treasury Department have already the machinery with which to arrive at the actual value of the capital of a corporation and if the definition of invested capital should be rewritten we submit that it can be arrived at in the same manner as the actual value of capital stock is determined under the provisions of Section 401 of the act of 1916. What I have stated here, indeed, is emphasized by the provisions of title 10 of the bill reported to the House by the Ways and Means Committee, wherein this identical tax is imposed, being increased, however, to \$1 instead of 50 cents on the fair average value of its capital stock.

But we, the manufacturers of proprietary medicines, are not asking that you shall set aside your present definition but are perfectly willing that you shall proceed upon the basis of capital invested irrespective of the actual value of the property, but we ask that in determining this actual investment, you shall give credit to us for the amounts of money which we have expended for constructive purposes. We have made a careful survey of this matter, and think we can state to you with a reasonable degree of accuracy that the money which is expended for advertising can be approximately divided into two classes, two-thirds of this money being expended for sales expense and one-third for constructive purposes. That is to say, that one-third of the money which has been expended for advertising goes directly into the value or cost of purchasing the value with as great a degree of certainty as money which would be expended upon a building which would be erected upon a vacant lot and, therefore, we

respectfully ask that if the definition of invested capital shall remain, there shall be modifications that the manufacturers of trade-mark goods shall be permitted to include, under such rules and regulations as may be published for the enforcement of the act, that part of the money which has been permanently and constructively invested in trade-marks and to receive the benefit thereof in arriving at the basis for the computation of the amount of taxes to be imposed upon our income.

Of course the Secretary of the Treasury must be satisfied, just as under the present law the Secretary of the Treasury must be satisfied by proper evidence of the amount of capital necessarily retained or used in the business for the purpose of determining the point at which 10 per cent will be imposed on undivided profits.

Permit me at this time to show you that the manufacturers of medicines are now paying and, under any system of taxation, will pay, a larger revenue than any other group of manufacturers. Alcohol is a necessary and essential ingredient in medicines, either for the purpose of extraction, solution, or preservation, and we are compelled to pay a direct tax upon alcohol which the bill pending in the House proposes to increase to \$4.40 per proof gallon, or approximately \$8.20, per wine gallon.

The tax proposed on alcohol for nonbeverage purposes would amount to about ten times the cost of the alcohol itself.

An illustration of the onerous character of this tax is found in the case of a manufacturer of an old, well-known household liniment used both for human beings and animals, which if it had paid a tax of \$4.40 per proof gallon on the alcohol used in 1917, would have paid the equivalent of 51.7 per cent of its gross sales. Other manufacturers of family remedies report their alcohol tax for their 1917 consumption if figured at \$8.20 per wine gallon, would have amounted to from 12 per cent to 32 per cent of their gross sales.

In many instances these preparations are marketed in dry form, the alcohol being used as a solvent and for granulation purposes. The tax on alcohol for medicinal purposes must be considered, in wine gallon units, \$8.20, as we are required to state the percentage of alcoholic content by volume under the provisions of the food and drugs act.

We respectfully submit that this is an unjust and unusual burden to be placed upon a raw chemical ingredient. Indeed, there is no more justification for such a tax upon one of the ingredients which enter into the manufacture of drugs than there would be for a special excise tax to be imposed upon any ingredient which entered into the manufacture of any substance. Indeed, we contend that there is less reason and justification in this instance for the reason that it is a tax upon an ingredient entering into the medicines of the sick. We ask only that this relief be granted for ingredients for the manufacture of such preparations as can in no wise be used for beverage purposes. Your attention is respectfully called to the fact that manufacturers using denatured alcohol do not pay a tax and we submit that there should be no difference in this regard between denatured alcohol, used as an ingredient, and alcohol used as an ingredient in the manufacture of medicines.

Permit me to say right here, that it is now and always has been my view that a necessity such as medicine ought not to be made the subject of special taxation. That there exists in my judgment no real excuse for the imposition of a tax of that kind.

If it be the judgment of this committee that a tax of this character should be retained, I have to respectfully submit my approval of the method of collection suggested by the Ways and Means Committee in the pending bill, namely by the affixing of a stamp by the vendor at the time of sale to the consumer and the reimbursement by the consumer of the amount of the stamp. We respectfully submit, however, that the amount to be raised by the pending bill is double that of the act of October 3 1917, under which was imposed a manufacturer's tax of 2 per cent and that if you substitute a 4 per cent tax at the time of the retail sale, the consumer to pay it at the time of the purchase, the revenues which the Government will obtain from the sale of these proprietary articles will be nearly five times the present receipts. The amount which the consumer pays will be only equal to the tax imposed and not a larger amount, which may result from the manufacturer passing it on to the jobber and the jobber to the retailer, and there will be less trade irritation.

Respectfully submitted,

FRANK A. BLAIR.
President of the Proprietary Association.

The CHAIRMAN. Senator Penrose says there is a gentleman here who will take only about two minutes.

Senator PENROSE. Mr. Horace Stern.

The CHAIRMAN. How long will it take you, Mr. Stern? The Senator from Pennsylvania suggests that it will only take you two minutes.

Mr. STERN. I think I can do it in two minutes.

The CHAIRMAN. Very well. We will give you five minutes.

STATEMENT OF MR. HORACE STERN.

Mr. STERN. Very well, Mr. Chairman. I wanted, if I might, to say a word in reference to section 1007 of the bill. This is on page 149. It reads as follows [reading:]

SEC. 1007. That on and after January 1, 1919, every manufacturer of automatic vending or weighing machines who operates such machines shall pay annually a special excise tax equivalent to 5 per centum of the gross amount received by him from such operation during the preceding year ending June 30.

Senator PENROSE. In order to get the record straight, Mr. Stern, may I ask you to state whom you represent?

Mr. STERN. Yes; the Harn & Hardart Automat Co. of Pennsylvania, operating automatic restaurants in the city of Philadelphia.

The CHAIRMAN. Go ahead.

Mr. STERN. Section 1007 puts a tax of 5 per cent on the gross amount received from the operation of automatic vending or weighing machines when they are operated by the manufacturer. Now, it happens that this Philadelphia Automat Co. does manufacture its own machines. My thought was that when the clause was put in it was intended to apply to machines selling luxuries, such as chocolate and chewing gum and things of that kind, and that the draft men of the bill never intended that it should apply to food, because an automat restaurant, selling food, is in many respects a public benefactor. It does away with the necessity of waiters, and it is sanitary. The competitors of the company I represent who do not use automatic vending machines would not be obliged to pay this tax, for example, such well known places as Childs', that operate these cheap restaurants.

Senator THOMAS. Did you say they operated cheap restaurants?

Mr. STERN. As cheap as anything can be nowadays. It is cheaper than the Willard and the Shoreham, and places of that kind.

Senator PENROSE. You mean that the Childs concerns do not manufacture the automat machinery, or they do not operate it?

Mr. STERN. No, sir; they do not operate the machines. I do not know if the Senator has ever indulged in that kind of an orgy or not. You go up to one of these machines and put a coin in a slot and there comes out a sandwich, or coffee, or any other article for which you put in a coin. [Laughter.]

I saw the Treasury Department in reference to this, and I saw Dr. Adams, who I believe originally suggested the draft of this bill, and in a letter written by him to Mr. Morris Wolf he says that the automatic restaurant was not thought of when the bill was drafted. I would like this letter to go in the record.

(The letter referred to is here printed in full, as follows:)

TREASURY DEPARTMENT,
Washington, July 27, 1918.

MORRIS WOLF, Esq.,

1118 Real Estate Trust Building,
Philadelphia, Pa.

MY DEAR Mr. WOLF: In reply to your letter of July 24, 1918, I am frank to say that the automatic restaurant was not in mind when the suggestion of a tax of 10 per cent of the gross collections on sales of all articles made by automatic vending machines was incorporated in the memorandum sent to the chairman of the Ways and Means Committee.

I am sending your letter together with a copy of my reply to Mr. Kitchin.

Yours, very truly,

T. ADAMS.

Mr. STERN. We caught this thing rather late. I notice that while originally the tax was put on the proceeds of sales from all automatic vending and weighing machines, it is restricted now to apply only where the manufacturer himself operates the machine. I do not know what the reason for that distinction was, but it hits only the company in Philadelphia. There are Horn & Hardart concerns in Chicago, New York, and Boston, but those are not affected because they do not operate their own machines.

Senator PENROSE. This clause discriminates between the operator who is the manufacturer of his own machine and the operator who is not the manufacturer?

Mr. STERN. Yes. On page 29, line 9, it provides a tax of 10 per cent for vending and weighing machines on the selling or leasing price when the machine is sold or leased. In other words, if a man sells or leases one of these automatic slot devices, weighing or vending machines, there is a tax of 10 per cent on the selling price or leasing price, but if the manufacturer operates the machine he pays a tax not on the cost of the machine, but he pays a perpetual tax of 5 per cent on the income derived from the operation of the machine. That seems to me to be rather an unusual discrimination.

Senator PENROSE. I can not see why such a distinction should be made, even on the chewing gum apparatus, not to mention the restaurant. Why a distinction at all?

Mr. STERN. I do not see it, either; but, of course, I was trying to confine the argument to the special point, that it was never intended to tax food. We feed forty million people a year, so that it is quite an item.

Senator PENROSE. You eliminate the tip system with the automatic waiter also, do you not?

Mr. STERN. Yes, we eliminate that, too. It has a great many advantages, as you can see by reason of the fact that a city with a population of two million sends forty million people a year to patronize it. It is very popular, and the company has many places in Philadelphia, and it seems to me a hardship that a cheap food concern—if I may so call it—selling to so many people and selling only the vital necessities of life, should be so taxed. It indulges in the sale of nothing more luxurious than ice cream. It seems to me a hardship not only that it should be subjected to a tax, but that it should be subjected to a tax only because it sells its food in a sanitary manner, not using man power, or even woman power, for that matter; and I do not think it was intended that the tax should be applied in

that way; and this apart from the suggestion that Senator Penrose makes, that it is an unfair discrimination against the manufacturer who is also the operator. I think that in line 19, if after the words "vending machines" the words "excepting automatic restaurants," were inserted, it would confine it to vending and weighing machines for everything but food.

Senator PENROSE. I think if you will introduce your system here in Washington you will have a great deal of patronage.

Senator THOMAS. I think the burden of proof is with him.

Senator PENROSE. The high cost of living has not affected these restaurants since they raised their prices, has it?

Mr. STERN. No; we can not raise our prices even if we were tempted to do so, because the machines are made for a certain sized coin. [Laughter.]

Senator THOMAS. This is one of the cases where mechanics prevents profiteering.

Mr. STERN. Yes.

Senator THOMAS. I think you ought to be exempted in this case.

Senator PENROSE. You could cut down the amount that comes out of the machine.

Mr. STERN. You can do that, yes; but you can not do that beyond the point where you have to satisfy a hungry man. Of course, we cater to the working masses who want to appease hunger rather than to satisfy fastidious tastes.

Senator THOMAS. You have made a pretty convincing argument, and I think you had better not go on.

Senator PENROSE. You do not use it in other restaurants?

Mr. STERN. No, sir; we use it only for our own purposes in our own restaurants. So far as I know this machinery is used only in Boston, Chicago, Philadelphia, and New York. The Philadelphia company makes the machines and operates them.

The CHAIRMAN. Why do you not make the machines and sell them to everybody?

Mr. STERN. In other cities?

The CHAIRMAN. Yes.

Mr. STERN. It requires, of course, capital, and we had it in mind to extend the system, but we went lately before the body that controls the issue of stocks and bonds, I forgot the technical name of it.

Senator THOMAS. The Priorities Committee?

Mr. STERN. No, the Capital Issues Committee, and we wanted more capital. Of course the extension of those restaurants is not so vital as compared with some of the bigger phases of the war interests, but we think this is a time when the extension of the system might be considered, and I may say in every city where it has been introduced it has met with success after people have become used to it. It was opened in Chicago a year ago.

Senator McCUMBER. Is it used in Washington?

Mr. STERN. No, sir. It originated in Philadelphia, and then it went next to New York and to Boston, and lately to Chicago.

Senator PENROSE. I should think it would do well in Washington. The committee would go there.

Senator McCUMBER. You might locate one in the Willard.

Senator THOMAS. Put one in the Senate restaurant.

(Mr. Stern at this point submitted two letters, which are here printed in full, as follows:)

WASHINGTON, D. C., September 18, 1918.

The WAYS AND MEANS COMMITTEE,

House of Representatives.

The FINANCE COMMITTEE,

United States Senate.

GENTLEMEN: The war-service committee of the Sanitary Drinking Cup Manufacturers' Association respectfully urge that sections 900 and 1007 of H. R. 12863 be amended so as not to apply to vending machines selling sanitary paper cups, for the following reasons:

1. Sanitary paper drinking cups cooperate with the United States Public Health Service under the Treasury Department regulations and also under the various State laws, which have abolished the infectious common drinking cups in preventing the spread of venereal and communicable diseases.

2. We supply hospitals, hospital ships, hospital supply bases, American Red Cross divisions, Navy supply depots, Army post exchanges, Young Men's Christian Association branches, factories, schoolhouses, railway trains, Government departments and bureaus, and public places in general.

3. This Nation is now confronted with the scourge of venereal diseases, as indicated by investigations of health officers of five training camps in different parts of the country, which show 32 per cent of the boys entering these camps were infected with venereal diseases, all of which may be contracted through the use of common drinking cups.

4. Surg. Gen. Rupert Blue, of the United States Public Health Service, says in the attached letter:

"This industry is in existence largely because of the necessity, in the interest of the public health, for the abolition of the common drinking cup. The product of this industry is a sanitary necessity essential to carrying out Federal and State laws forbidding the use of the common drinking cup. The work of the United States Public Health Service and of the State and municipal health departments in preventing the spread of communicable diseases can not be efficiently continued unless an ample supply of these paper drinking cups is assured."

5. A few paper drinking cup vending machines might stand such a tax, but the great majority would not pay and be abandoned.

Instead of taxing them out of existence, an appropriation ought to be made by the Government to extend their use for the purpose of protecting the public health.

We respectfully request, in view of the foregoing facts, that sections 900 and 1007 be amended so as not to include sanitary cup vending machines or that the matter be submitted to the Surgeon General of the United States Public Health Service for his opinion thereon.

Respectfully submitted.

WAR SERVICE COMMITTEE OF THE SANITARY DRINKING
CUP MANUFACTURERS' ASSOCIATION,

L. W. LUELLEN, *Chairman,*

220 West Nineteenth Street, New York City.

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TREASURY DEPARTMENT,

OFFICE OF THE SURGEON GENERAL, PUBLIC HEALTH SERVICE,

Washington September 6, 1918.

THE PRIORITIES BOARD OF THE WAR INDUSTRIES BOARD,

Washington, D. C.

GENTLEMEN: There has been referred to me by the pulp and paper section of the War Industries Board for "comments, suggestions, and possible indorsement" the question of the classification of the industry of making individual paper drinking cups.

This industry is in existence largely because of the necessity in the interest of the public health for the abolition of the common drinking cup. The product of this industry is a sanitary necessity essential to carrying out Federal and State laws forbidding the use of the common drinking cup.

The work of the United States Public Health Service and of the State and municipal health departments in preventing the spread of communicable diseases can not be efficiently continued unless an ample supply of these paper drinking cups is assured.

I have the honor, therefore, to indorse the application of the committee of the Sanitary Drinking Cup Manufacturers' Association that their industry be indorsed as essential in order that they may secure the materials and substances necessary for the manufacture of sanitary drinking cups.

Respectfully,

RUPERT BLUE, *Surgeon General.*

Senator PENROSE. I desire to file for the record a brief submitted by Mr. Stern on the automatic restaurant proposition.

(The brief referred to is here printed in full, as follows:)

TAX ON AUTOMATIC VENDING MACHINES.

[Section 1007 of proposed revenue bill.]

The CHAIRMAN OF THE SENATE COMMITTEE ON FINANCE,
Washington, D. C.

DEAR SIR: On behalf of the Horn & Hardart enterprises in Philadelphia, New York, Chicago, and Boston, we beg to submit the following argument in favor of the exemption of automatic restaurants from the provisions of section 1007 of the proposed revenue bill, which section reads as follows:

"That on and after January first, nineteen hundred and nineteen, every manufacturer of automatic vending or weighing machines who operates such machines shall pay annually a special excise tax equivalent to five per centum of the gross amount received by him from such operation during the preceding year ending June thirtieth."

1. In July, 1918, the Treasury Department submitted to the Ways and Means Committee of the House of Representatives a memorandum of possible sources of revenue secured from taxes on "luxuries and nonessential expenditures." In the memorandum the department stated that the taxes which it suggested were designed "not only to raise additional revenue but for the equally important purpose of discouraging wasteful consumption and unnecessary production," and further that "the really needy consumer is amply protected by exempting from the tax altogether those classes of articles which the poor actually buy or need to buy." Among the taxes proposed was a tax of 10 per cent on the sales of all articles made by automatic vending machines.

2. The general language of this recommendation appeared to include the automatic restaurants, known as "automats," operated by the Horn & Hardart enterprises in Philadelphia, New York, Chicago, and Boston.

These automats are large restaurants centrally located, in which, instead of securing food from waiters or from exposed counters, the food is kept in closed glass compartments, and the patrons, by dropping a coin beside the compartment containing the article of food which they desire, are enabled to unlock the glass door and take out the article of food.

The advantages of this method of selling food are: First, it is highly sanitary, because the food is not exposed to the air or handled by waiters when delivered; and, second, that by avoiding the necessity for service in delivering the food there is a saving of time, an avoidance of the necessity for tipping, and an economy in the number of employees required.

As a result of these advantages, the enterprises have grown from a small restaurant operated by Mr. Hardart in New Orleans to 48 establishments in the business centers, which take care of about 40,000,000 patrons a year. That these patrons are of the working classes is evident from the fact that the average expenditure per person per meal is under 15 cents.

3. A consideration of these facts made it evident that the Treasury Department did not mean to include the automats in the luxuries list, and when the matter was taken up with the Treasury Department that department stated in a letter which has been presented to the committee, and which is in its record, that automats were not in contemplation when the 10 per cent tax was suggested to the Ways and Means Committee.

4. Accordingly the Ways and Means Committee did not include in the bill which it passed any such provision as was embodied in the memorandum from the Treasury Department.

It did suggest a tax of 10 per cent on the sales price of automatic vending machines. (Sec. 900, par. 21.) This tax we consider entirely fair.

In section 1007, however, quoted at the beginning of this brief, a tax of 5 per cent was laid on the receipts of automatic vending machines operated by the manufacturers. No tax was laid on such machines not operated by the manufacturers, nor was the tax limited to machines that should be manufactured after the date of the passage of the bill.

5. When Mr. Horn and Mr. Hardart adopted the idea of the automats, such machines were not built in this country, and in order to secure them they were compelled to build machines themselves. The result is that they now operate many machines which they built, some many years ago and some more recently.

A tax of 5 per cent of the receipts of these machines would be prohibitive, as the Horn & Hardart restaurants have to compete with other popular priced restaurants, such as Childs's and Thompson's, whose receipts are not taxed in any way.

In these disturbed times the profits of the business in most cases do not amount to nearly 5 per cent of the receipts, and the result of the passage of the bill in its present form would be that Horn & Hardart would have to go back to the selling of their food by waiters, thereby sacrificing the cleanliness and saving which the automat machine secures. As far as they are concerned, therefore, the tax would not produce revenue for the Government, but would simply cause a return to less efficient methods of selling the food.

6. We therefore ask that if the new bill embodies any tax on automatic vending machines, it except automatic restaurants, by adding the words "except automatic restaurants" after the words "automatic vending or weighing machines," in section 1007.

Respectfully submitted.

STERN & WOLF.

SEPTEMBER 13, 1918.

Senator McCUMBER. Before we adjourn, Mr. Chairman, I would say that I received a telephone message from Chicago last evening, indirectly coming from Congressman Britten, of Chicago, who wanted to be heard Friday or Saturday, and wanted to try to fix a time. I could not call you up, and I told him that I was certain, if he wished to be heard, he could be heard Friday afternoon.

The CHAIRMAN. Does the Congressman want to be heard?

Senator McCUMBER. Yes, I presume so; I understand so.

The CHAIRMAN. All right, we will hear him.

(Thereupon, at 1 o'clock p. m. the committee took a recess until 3 o'clock p. m.).

AFTERNOON SESSION.

The committee reassembled at 3 o'clock p. m., pursuant to taking the recess.

The CHAIRMAN. The committee will next hear Dr. Klein. Dr. Klein state what interests you represent and what you wish to speak about in the bill.

WAR PROFITS TAX.

STATEMENT OF DR. JOSEPH J. KLEIN, NEW YORK.

Dr. KLEIN. I represent no interest. I am tax editor for a New York newspaper. I am a certified public accountant, and represent a number of tax-paying entities—corporations, partnerships, and individuals. But I appear here in my private capacity, representing no interest whatsoever without retainer.

Senator PENROSE. In what business are you engaged?

Dr. KLEIN. I am a certified public accountant in New York City.

Senator PENROSE. To what phase of the bill do you address yourself?

Dr. KLEIN. I am going to speak, if I may have a few minutes, on the possibility of removing the excess profits and the alternative war profits tax provision applying, as it does in the proposed bill, to corporations only, and in favor of some consumption tax that I previously brought to the attention of the Ways and Means Committee.

The CHAIRMAN. How much time do you want?

Dr. KLEIN. Within 15 minutes unless you wish to keep me longer.

Senator PENROSE. Did you have a hearing before the Ways and Means Committee?

Dr. KLEIN. I did; they gave me 15 minutes and kept me there for about an hour and a half.

Senator PENROSE. Then you simply want to repeat what you stated to them?

Dr. KLEIN. No, sir, because at that time the restriction of the excess war profits tax to corporations only was not thought of.

Senator McCUMBER. If he can give us some new subjects of taxation, I think we should give him all the time he wants.

Senator THOMAS. I understand you want to argue for the extension of these profits to others than corporations?

Dr. KLEIN. No, sir; just the reverse. I propose to point out a way to do away with those profit taxes entirely. I will try to develop that thought.

Senator SMOOT. That is, you mean excess profits?

Dr. KLEIN. Yes; and the war profits tax.

Senator PENROSE. You want to advocate consumption taxes.

Dr. KLEIN. No, sir; but to make it easy to do away with the other taxes.

The first matter, the application of the corporations' profit tax, including both the excess profits and the war profits, has been retained, in my opinion, whether consciously or unconsciously, by the committee on the other side of the Capitol, because there has been no practical means found thus far to force a corporation to distribute its earnings. The attempt was made in the bill of October 3, 1917, to compel that distribution by the tax on undistributed profits. One of the deputy commissioners is of the opinion that very little, if anything, will ever be collected under that provision of the law.

In the present proposed law the 18 per cent on corporation profits, compared to the 12 per cent on the profits that remain after payment of dividends, is another attempt to force the distribution of corporation earnings.

I take it that every thinker on taxes will agree that if there were only some means available whereby every organization, regardless of the form of the organization, regardless of the proprietary form—individual, partnership, or corporation—if each one of these forms of organization could be made to pay a tax depending exactly on some basic factor—capital the poorest of all factors, earnings probably the best factor—I believe that we would grasp at the opportunity so to tax.

So I propose as an alternative proposition to the proposed excess profits tax at the higher rates than proposed by the Secretary of the Treasury, and for the alternative war profits tax, based, as it is, upon the British provision, a compulsory distribution of corporate earn-

ings applicable to the year in which they are earned, and not to the year in which declared—and I will make that clear in a moment—of at least 25 per cent in cash, and the balance in script, and the provision for the minimum of 25 per cent is a very poor attempt on my part to strike an average of the amount payable in cash to the Government by each shareholder on the assumed basis of his share of corporate profits.

Pardon this illustration. I think it will make it clearer. In a partnership consisting of five or six individuals, each partner is presumed to have full possession, in law and in fact, of the share of partnership profits to which his interest in the entity entitles him. He reports that share of profits in his individual income tax return, and then he must seek some way of paying the tax bill, despite the fact that he may not have those profits distributed to him in cash, because the organization, the partnership must retain some of its earnings for future development, for renewals of its activities, and so on. Despite the fact, however, that in many cases the partnership, as such, does not distribute its earnings, the individual partner is supposed to have received the profits, a share of the profits, to make his return and to pay the tax thereon.

In a close corporation, consisting, let us say, of the same number of shareholders, on an assumption which may or may not be constitutional, but, in my opinion, is at least as constitutional as the tax on the salaries paid to State officials and employees, and municipal officials and employees, for which I was somewhat responsible on the other side of the Capitol, I feel that by assuming that corporations' profits are distributed, merely on the basis of having been earned, to individual shareholders, we would attain the object that tax legislators have been trying to reach for years, now, namely, to force a distribution of corporate earnings; and if you do so legislate that a corporation's earnings shall assume to have been distributed, you place on an absolute par, on an absolutely equitable relationship, one as to the other, all partnerships, all individuals, and all corporations. Of course, the thought could be developed to greater length, but I think I have presented the basic idea and I am willing to leave it with you, unless you wish to ask questions regarding it.

Senator Smoot. Do you mean 25 per cent of the earnings of all partnerships, corporations, and individuals, should be paid as a flat tax to the Government?

Dr. KLEIN. No, sir. I propose that at least 25 per cent of the corporations' earnings shall be paid in a cash dividend to the shareholders so as to enable those shareholders to meet their tax bill, based upon such earnings.

Senator Smoot. There is more than 25 per cent now.

Dr. KLEIN. Yes, sir, 25 per cent, plus the flat 12 per cent income tax, would make it 37 per cent, and I am merely guessing on the amount that is required to be distributed. You have a statistical department at the Treasury Building. I see Mr. McCoy here. They have available the data which is not mine. I know in some cases the amounts distributed will be entirely too large, in other cases entirely too small. But, of course, the whole provision is a war expedient, and the only economic objection I have ever come across re-

garding corporations' profits as having been distributed to shareholders, is the fact that you then call upon shareholders in a corporation to pay a tax without giving them the means with which to pay that tax. They are not presumed to be placed in possession of the profits until by action of the board of directors, or corresponding body, the dividend has been declared, of course.

Senator THOMAS. They do not pay a tax on their income until they receive it.

Dr. KLEIN. That is exactly what I am trying to say. I am trying to provide a means whereby every organization, including corporations, will pay the full measure of tax, based upon earnings for that year. At the present time I have tried to approximate the relationship between an individual's tax, a partner's tax, and a corporation tax, and I find that there is a close approximation, so that those who developed the scale of rates, built well. Of course, there are extremes.

Senator THOMAS. I do not understand you. My impression is that what you are arguing for is to relieve the corporations from the burden of the excess and war profits tax by shifting it upon the individual stockholders, and then giving them a guaranteed cash income from the corporation in which they are stockholders of not less than 25 per cent of the earnings.

Dr. KLEIN. Yes, sir.

Senator THOMAS. And then increase the tax upon the stockholders. Is that correct?

Dr. KLEIN. To have the stockholder's tax on the same basis as any other individual's tax. My bigger point there is that every organization, regardless of its form, which is an incident, should pay the same tax based upon its earnings.

Senator SMOOT. The result would be, you would desire to raise money by income rather than by excess profits?

Dr. KLEIN. And one reason for that, Senator, is that everybody is agreed that the artificial excess profits tax is inequitable.

Senator SMOOT. No doubt. Everybody knows it.

Dr. KLEIN. I am trying to propose an exemption which would be more equitable in this. No real patriot objects to high taxes. He objects to what he believes at times to be inequitable burdens, incidents that are not fair. I am trying to make the incidents of the taxes fall equally upon every taxpayer, and that is a consummation much to be wished.

Senator THOMAS. If you can do that, you will be entitled to a monument.

Senator McCUMBER. If we had a system that would be far more equitable, what effect would it have on the amount of taxes that would be raised, after you make your allowances for exemptions to individuals, which would not be allowed, of course, to corporations?

Dr. KLEIN. A few moments ago I took a corporation, a partnership, and an individual, with invested capital of \$100,000, and earnings of various amounts, and a rough approximation showed me that the amounts to be paid by each of these organizations does not radically differ in any case due to corporate organization, except in this, the provision in the law frees from normal tax dividends. But here is what actually happens. Corporation A has paid an excess profits or war profits tax of \$90,000, and an income tax of \$10,000 and

then has a balance of profits of \$30,000 or \$40,000, or \$50,000, which it ought to, of course, and sometimes does, actually distribute to its shareholders. Those shareholders then pay surtaxes, but do not pay any normal tax, on the assumption that the corporation has already paid a 12 per cent normal tax on the earnings distributed. But the fact remains that had this distribution to A, B, and C been made through a partnership, or to A himself through his own business, the war profits and the excess profits tax would not have applied.

Senator McCUMBER. But here is the point I make. Suppose a corporation makes \$100,000 net profits, it is taxed upon those net profits under the present system.

Dr. KLEIN. Yes, sir.

Senator McCUMBER. Suppose that is divided, however, among a hundred stockholders, and each of them receives a thousand dollars, and each one claims his exemption of \$1,000. Then the Government gets no tax. That is the point.

Dr. KLEIN. That is right. I show that that is not an undue hardship, due to this fact, that if in a partnership the same condition existed, then the partners pay the smaller tax, and if it is fair in a partnership, it is surely no less fair in a corporation. I do not believe anybody, surely on this side of the Capitol, wants to strike at a corporation merely because it is a corporation.

Senator McCUMBER. I was not speaking of the fairness of it. I was asking what effect it would have on the amount to be received.

Senator THOMAS. I am not so sure about that last proposition. Nobody has ever accused me of being a friend of the corporations, particularly. But I cannot understand why this war profits and this excess profits is limited to corporations.

Dr. KLEIN. My point is this, Senator, if the war profits and the excess profits taxing is basically good, it ought to apply to every line of business, and if it applies to corporations only, the only economic reason for it I can find is because it is so hard to get at the profits of a corporation.

Senator THOMAS. I think there is a political reason behind it, myself.

Senator SMOOT. How are you going to make up for the loss in in taxes if we adopt your suggestion? Because if your suggestion is adopted, we have to find other sources to collect at least \$2,000,000,000.

Dr. KLEIN. I will give you from two to four billions in this way. One of the striking features of the last excess profits tax, in so far as it related to the individual taxpayer, was the difficulties encountered in interpreting that law. That was the difficulty that the taxpayer experienced and the Treasury Department experienced. They had to call in outside help, and they threw up their hands, and the outside help threw up their hands. The remarkable part was that this artificial tax netted less than one per cent of the net sales of the country. One of the most difficult statistical figures to obtain is the turnover of the volume of business done in the country. I have estimated it to be more than two hundred billions of dollars.

Senator SMOOT. You are too high.

Dr. KLEIN. The 1917 figures are as follows. The result of mining. The value of mining products produced \$3,000,000,000; of building operations and materials, \$1,000,000,000, and of farm

products, \$40,000,000,000. Those figures, taken from the "Statistical Abstract," refer to initial or original factors. Take, for example, the price of wheat is included here, but not the value of the flour or the value of the products of the flour. The steel and iron figures are here, but not the value of the beams, and rails and so on. In ordinary business there are at least three hands through which product flows from the initial stage until the consumption stage, and so these figures of \$63,000,000,000, not including transportation, not including communication of any sort, and not including rents and leases, amount to \$63,000,000,000, and I have taken the factor of three, which gives us approximately \$200,000,000,000 for 1917. Whether the figures will be increased or decreased for 1918 I have no means of knowing now.

Senator SMOOT. I think you are about \$750,000,000,000 too high.

Senator LODGE. Do you mean the turnover and all?

Senator SMOOT. Yes. That is not over 100 per cent.

The CHAIRMAN. I think we pretty fairly understand your proposition, Mr. Klein.

Dr. KLEIN. Give me just two more minutes, and I will give you the sources of other taxation that you have not had. The 2 per cent on what I have given you would give you anywhere from two billions to four billions. The other consumption taxes I have not presented are the following. I thought this first one would be accepted by the House, but for some reason or other it was dropped. One is a tax on telephone messages, 5-cent and 10-cent calls. There is a tax on 15-cent calls. That would net, I estimate, 150 millions of dollars.

Senator SMOOT. Five cent calls?

Dr. KLEIN. Five cent and 10 cent calls, not including subscribers calls, would net 150 millions of dollars. There are 20,000,000,000 telephone messages of which we take one-fourth to be toll messages and uncontrolled. A flat tax of 2 cents on mercantile invoices or bills would yield, I estimate, thirty millions of dollars. Why the tax on checks was ignored I can not find any reason for. In our Civil War and our Spanish American War we had that tax. A flat tax of 2 cents would yield \$30,000,000. A flat tax of 3 cents—

The CHAIRMAN. We have all that data, and have been over it repeatedly. You need not bother about it.

Senator THOMAS. Suppose you put your statement in the record, and then we can get it.

Dr. KLEIN. That is all, then, Mr. Chairman. I thank you.

The CHAIRMAN. Your proposition is simply to substitute a tax upon the undistributed earnings of corporations that now escape taxation, as a substitute for the excess profits and the war tax?

Dr. KLEIN. Assuming that the distribution has been made as in a partnership.

The CHAIRMAN. Assuming the distribution has been made, and provide for forcing it to be made.

Dr. KLEIN. Yes, sir.

The CHAIRMAN. The substance of your proposition, after you have eliminated all the machinery, is that we will provide a method by which what is now known as the undistributed earnings of corporations will be compelled to pay the income tax we impose?

Dr. KLEIN. Exactly.

The CHAIRMAN. And you propose that as a substitute for the excess and the war profits.

Dr. KLEIN. Yes, sir.

(The chairman submitted a petition from the New York Board of Trade and Transportation, which is here printed in full, as follows:)

NEW YORK BOARD OF TRADE AND TRANSPORTATION,
New York, September 17, 1918.

To the FINANCE COMMITTEE OF THE UNITED STATES SENATE, and the
COMMITTEE ON WAYS AND MEANS OF THE HOUSE OF REPRESENTATIVES,
Washington, D. C.

(GENTLEMEN: The undersigned fully comprehend the perplexing nature of the problems which confront your committees in their efforts to prepare the law under which the moneys that are necessary to carry on the war shall be raised. We sympathize with you in your arduous labors and, therefore, the suggestions herein are made in no spirit of criticism, but with the same inspiration of loyalty to our country which we are confident actuates your members.

1. We believe that under the pending bill the sum to be raised by taxation during the year is too large in proportion to the amount to be raised by the sale of bonds. It is unnecessary to place so large a share of the burden of cost upon the present generation who are fighting this war by their man power. The greater benefits which are to be achieved will be enjoyed by posterity who should in justice carry a large share of the cost.

2. At no time should taxation reach a height which will make it impossible for any part of our people to take their proper share in subscribing for liberty bonds. Under the pending bill persons with the largest incomes and paying under the highest surtaxes will find their current income and their power to purchase bonds seriously curtailed.

It is proposed to put every available dollar into the war. It is proposed to raise \$8,000,000,000 by taxation and \$16,000,000,000 by bond sales. These bonds must be purchased and these taxes paid out of the available cash resources of the Nation.

The larger purchasers of bonds are those having the larger resources. But under the pending bill these larger resources are taxed as high as 70 per cent, which leaves a total of only 30 per cent of such resources available for bonds.

3. The bill is avowedly based upon the principle that those who are best able to pay shall pay. This principle is worked out in the bill to such an extreme as to become not only inequitable but unwise, because it will deprive the great mass of our people from carrying any adequate part of the financial burden. The law should recognize the principle that it is the patriotic privilege, as well as the duty, of every American citizen, and of every other person who enjoys the unparalleled advantages of living under our American conditions and institutions, to contribute to the extent of his ability whether much or little. Taxes should be so levied as to give the smallest wage earner an opportunity to contribute something and such distribution of the tax to the entire community would make the burden light for all and impose no unjust share on any.

4. No extra tax should be placed upon undistributed earnings of corporations, as such tax would foster bad finance and compel distribution of larger amounts than would be safe for the corporation and would make it difficult or impossible to provide the capital necessary for the protection and extension of the business.

In this connection it must be borne in mind that the present high cost of labor and of materials make the cost of production several times greater than before the war, and, therefore, necessitate a much larger working capital. This condition affects the whole business interests of the country alike, financial, commercial, manufacturing, and agricultural.

Nothing should be done that will curtail industry, for the Government has no other resources than the combined resources of the people of the Nation, and the people have no resources other than the returns from the active industries in which they are engaged, and such industries must be fostered and encouraged or their revenue-yielding power will dwindle or lapse.

Any unusual or extra tax upon undistributed earnings of corporations, therefore, would be dangerous and unwise and lead to disaster.

5. None of the available sources of revenue should be neglected, and the distribution of the burden should be made as broad and general as possible. We

therefore recommend a stamp tax on bank checks and on receipted bills or invoices. We also believe that a general consumption tax of a very small percentage should be imposed and collected through the retail seller.

All persons receiving an income of \$1,000 and less should pay a tax of at least 1 per cent, which could be collected with small expense through the internal-revenue officers or the local post office.

If incomes of \$1,000 and less should be taxed the exemption of \$1,000 now allowed should be repealed and the normal tax rate of 6 per cent reduced proportionately upon incomes of up to \$4,000, in order that there shall be no inequalities or inconsistencies, and to avoid making the tax on such incomes excessive.

Respectfully submitted.

J. FREDERICK TALCOTT, *Chairman*.
FRANK BRAINARD,
JOSEPH H. EMERY,
NATHAN T. PULSIFER,
STEPHEN FARRELLY,

Special Committee on War Revenue,
New York Board of Trade and Transportation.

LEE KOHNS, *President*.

A true copy.

FRANK S. GARDNER, *Secretary*.

The CHAIRMAN. You may be heard now, Mr. Bond.

NONBEVERAGE ALCOHOL.

STATEMENT OF MR. RICHARD H. BOND, OF BALTIMORE, MD.

Mr. BOND. Mr. Chairman, I represent the Flavoring Extract Association of the United States. I desire to speak to the raising of the tax on nonbeverage alcohol as applied to flavoring extracts.

Gentlemen, it is a conceded fact that flavoring extracts are a necessity in the modern world. You gentlemen would all know what a flavorless dietary would mean. The United States Government also recognizes the necessity of flavoring extracts in the dietary of the Army and of the Navy, and is today the largest single purchaser of extracts in the world. You have the data before you gentlemen, I have no doubt, of their purchases of these items for use in the Army and Navy. Due very largely to that fact, our men composing the Army and the Navy are the best cared for Army and Navy in the world, particularly in their dietary.

The food authorities are continually asking our people to conserve food and not to waste food. The flavoring extract is the most important factor in permitting the people to conserve and not waste other things that formerly would have been thrown away. In the average household I believe you gentlemen who know of these things and come in direct contact with the rank and file of the people know that they are now using foods that formerly went into the garbage can, and they are being used in advantageous and palatable ways, and very largely by the use of flavoring extracts.

Alcohol is a necessity in the manufacture of flavoring extracts. Manufacturers have tried, and scientists have, for many years, to find some other ingredient which will dissolve and hold in solution and extract the flavoring principles which are used for the flavoring of foods and what not. It is an absolute necessity.

Flavoring extracts are recognized as foods and necessities by the legislation of all of the States. The former cost of the alcohol used

in flavoring extracts was \$1.10 per proof gallon. That is about \$2.09 a wine gallon. We have to figure on the wine gallon. The last revenue act placed a tax of \$2.20 per proof gallon upon nonbeverage alcohol, of which flavoring extracts are made. That makes a tax paid to the Government figure about \$4.18 per wine gallon of flavoring extracts used.

I say to you that a comparison—and not selecting them for the high alcohol contents, but a few of the more popular ones—shows that they will average about 57 per cent alcoholic contents in all flavoring extracts per volume. Figuring on raising this tax to \$4.40, which we will have to pay on it, basing it upon the two-ounce package, at the price now received, it would make the consumer pay to the Government 42 per cent of the entire price which the manufacturer receives for the flavoring extract, basing it on an average of 57 per cent, selecting these flavors, and not selecting the high grade ones.

When you placed the tax on before, due to other conditions brought about by the war, the little six spoonsful, the six dram bottle, as we call it, had to be sold at 15 cents to the consuming public. With the placing of this tax of \$4.40 upon it, the consuming public will have to pay, more than likely, 25 cents, and certainly beyond 20 cents, for this six teaspoonsful of flavoring extract.

Senator THOMAS. What per cent of that is alcohol?

Mr. BOND. About 57 per cent.

Senator THOMAS. Do you not think a gradual disuse of these flavoring extracts would promote the cause of temperance?

Mr. BOND. I would say to you that the department has had that matter entirely in hand, for this reason, that we have to give bond to the Treasury Department that these flavoring extracts shall not be used for beverage purposes; also, that we are liable, and the men who sell these goods are also liable, to the State authorities in the prohibition States, if they sell these foods as beverages, or if they sell them under circumstances which would permit a reasonable man to believe they were going to be so used. And the people of the country ought not to be cut off by reason of the temperance propaganda from these necessary things of modern life.

Senator THOMAS. I just wanted to get your idea about it.

Mr. BOND. I believe a price of that sort would be prohibitory. I do not think a price of that sort ought to be placed upon this necessary article of the people's use.

Senator SMOOR. Is it your idea to make a special tax upon alcohol that enters into the extracts?

Mr. BOND. We are satisfied, and I believe that the people had adjusted themselves to the present price, \$2.20 per proof gallon.

Senator PENROSE. What kind of flavoring extracts are these? I was out when you began your remarks.

Mr. BOND. I said selecting a half dozen at random of the flavoring extracts, such as lemon and pineapple and strawberry, and not seeking those which contain a high alcoholic content, but taking the average.

Senator PENROSE. They are the popular ones?

Mr. BOND. They are the more popular ones; yes, sir. The largest sale of flavoring extracts is of vanilla and lemon. The South, even before the days of prohibition, bought about three times as much

lemon flavor as they used of vanilla flavor, and in the northern section of our country, also before, and in the middle section before that section went dry, they used about three times as much vanilla as they did of lemon, a difference in the dietary ideas among the people.

Senator PENROSE. Has the consumption increased since these territories went dry?

Mr. BOND. I can hardly refer to that as tonnage, but I would say that the volume of business, as represented by the price received for it, is slightly larger than before. Some of them are less. I would say, however, that the tonnage, so to speak, is smaller than it has been.

Senator McCUMBER. Do you think the housewife will cease to put vanilla in her cakes because she has to pay 25 cents where she used to buy it at 15 cents?

Mr. BOND. I think she will not make so many cakes. I think she will not take so many crusts of bread and make them into bread pudding, and the thousand and one things that go into these house economies.

GASOLINE.

The CHAIRMAN. Mr. C. G. Howes desires to be heard now. Proceed, Mr. Howes.

STATEMENT OF MR. C. G. HOWES.

Mr. Howes. Mr. Chairman, I represent the dying and cleaning industry of the United States. I would call your special attention to page 130 of the bill, section 902, excise taxes, regarding the imposition of a tax of 2 cents a gallon on gasoline.

Because of the peculiar use which we make of gasoline this tax, as proposed, probably unintentionally, is going to work a very grave hardship on us by placing a tax entirely out of proportion to our capitalization, our gross business, our net income, and our ability to pay. We do not seek, however, to have this tax entirely eliminated, as far as it enters into the consumption of gasoline as fuel, or as it enters as an ingredient or factor into some other product. But we do fear that this tax, which will be placed on this commodity which we use so extensively, is unwarranted and unjustifiable, and I am going to appeal to your sense of justice by showing you a few figures to bear me out in my contention.

Our investment is \$60,000,000. Our gross business is \$90,000,000. Our net profit, on the basis of 10 per cent, is \$9,000,000. We have 2,000 plants. Our capacity at present of gasoline for cleansing purposes only is 50,000,000 gallons. That is outside of the 5,000,000 gallons we use for motor delivery. Two cents tax on 50,000,000 gallons will be \$1,000,000, which will be 11 per cent on the net profit, and that will be about 2½ per cent of the entire return estimated from this source by the Ways and Means Committee—\$40,000,000.

Our industry as a whole, as an entirety, is really small compared with one factor in one of the larger industries which could well afford to pay three or four times this amount.

Senator McCUMBER. You use about a gallon of alcohol for cleaning one suit of clothes?

Mr. HOWES. A gallon of gasoline?

Senator McCUMBER. Yes.

Mr. HOWES. Hardly; I would say it would average that.

Senator McCUMBER. You think it would average a gallon?

Mr. HOWES. Yes.

Senator McCUMBER. Do you not think the consuming public could stand that 2 cents?

Mr. HOWES. I will tell you, Senator, that is just the point. The increase in materials since the war started, not only of gasoline, which has jumped from 11 cents to 20 and 26 cents, but the denial by the Government of ammonia and acids, which we used to supplement that work, has made us entirely reliant, for the most part, on gasoline. To meet that, and with the enormous increase in cost of labor and other factors, rents, and so forth, which have increased, we have got to charge our customers up to the very limit, where further increase will decrease the business.

Senator McCUMBER. If you charge an increase of almost a hundred per cent in labor, the point with me was that you could probably put 2 cents on it for gasoline.

Mr. HOWES. In fact, we have considered that very carefully, and feel that any just and equitable assessment of our charges to the public to spread it over would be impossible, because our charges are so small. Where you previously had to pay a dollar and a quarter to have a suit of clothes cleaned, it is now up to \$2, and it has gone as high as you or any gentlemen of ordinary means would care to put into having his clothes cleaned.

Senator PENROSE. Do you mean to state it takes a gallon of gasoline to clean a suit of clothes?

Mr. HOWES. I do.

Senator PENROSE. I had no idea it took that much.

Mr. HOWES. You take the fresh gasoline, and with the bath that is used, and then the rinse subsequently, and the evaporation, it takes about a gallon of gasoline.

Senator SMOOT. Just the cleaning and the pressing of a suit of clothes does not take a quarter of a gallon, does it?

Mr. HOWES. To have it thoroughly cleaned. The ordinary tailor, as you may notice, is not a fair representative of the capacities of our industries.

Senator SMOOT. Do you clean children's clothing?

Mr. HOWES. Yes; every manner of clothing and household articles. And I might mention here that the War Department has mentioned this industry as a most powerful factor in the conservation of wool.

Senator SMOOT. I am quite sure that you can not raise the price of cleaning now, because if it was raised just a little higher you could go and buy a new dress or a new suit for the amount you charge. I am positive of that.

Senator THOMAS. You speak from personal experience?

Senator SMOOT. I speak from the bills I get every month.

Mr. HOWES. I feel this way about it, really, that the tax could not be distributed equitably among all the people and in its effect on our industry it becomes a license to operate. In my particular business I use 25,000 gallons of fresh gasoline a year. That would mean a tax of \$500, and my tax is about \$700. That increases my contribution to \$1,200, which I feel is quite out of proportion to the importance of the industry.

We do not wish to evade our just proportion of the motor gasoline tax, and as it is now that tax would be \$100,000 with us. We use 5,000,000 gallons of gas for motor purposes, and it is our impression that it should either be 3 or 4 cents a gallon used for fuel purposes. That hits the agricultural people as well as motor people. But we feel that tax would be justifiable and equitably distributed. We want relief from the tax on gasoline as it pertains to cleansing purposes.

Senator McCUMBER. You now charge \$2. After this law goes into effect you would charge \$2.02. Do you think you would lose any business by that?

Mr. HOWES. I think we would have hard work convincing the people about it. They would haggle at this odd figure.

Senator SMOOT. They would just charge \$2.25.

Mr. HOWES. I do not want to take any more time. That is my main contention.

(The following brief was subsequently submitted by Mr. Howes, and is here printed in full, as follows:)

BRIEF PRESENTED TO THE FINANCE COMMITTEE OF THE UNITED STATES SENATE BY THE CLEANING AND DYEING INDUSTRY OF THE UNITED STATES, SEPTEMBER 12, 1918.

To the honorable, the Committee on Finance, United States Senate.

GENTLEMEN: The proposed tax levy of 2 cents a gallon on gasoline, as contained in section 902, Title XI, excise taxes, H. R. 12863, entitled, "A bill to provide revenue and for other purposes," occasions this protest from the cleaning and dyeing industry of the United States.

The cleaning industry utilizes gasoline in two ways:

1. As fuel for its motor delivery.
2. As the basic agent for its cleansing processes.

In so far as the tax applies to motor consumption for fuel, the industry heartily acquiesces, being willing to accept not only the proposed rate, but any other rate deemed advisable to bring the necessary amount of revenue from this source into its proper proportion to the whole.

We do not desire exemption from any tax, if that tax is equally and equitably distributed. What we earnestly oppose is what appears to us as double taxation. Our contention is based on these grounds:

1. In paying a tax on gasoline for motor or fuel consumption we share with others equally, proportionately, and come under the original intent of the law. This we most heartily indorse.

2. The payment of a tax on gasoline for cleansing purposes is an unjust added burden, taxing the principal ingredient used in our industry, in addition to that which we will share with the automobile users.

Because of the unprecedented increase in the cost of labor and other materials used in our industry, the present price for service to the public has reached a figure where it now has a tendency to discourage the individual of moderate income.

The following facts reveal the small size of the industry and the great importance of gasoline in its operation:

STATISTICS FOR 1917.

Number of plants	2,000
Invested capital	\$60,000,000
Total gross business	\$90,000,000
Estimated net profit, 10 per cent	\$9,000,000
Consumption of gasoline	50,000,000 gal.
The estimated total net revenue from all sources is	\$40,000,000
The tax on 50,000,000 gallons, our consumption, will yield	\$1,000,000
This \$1,000,000 shows a ratio to the whole tax of	2½%
This \$1,000,000 represents 11% of the net income of this industry	11%

This is a levy entirely out of proportion to the capitalization, gross business, and net return of this industry; it is an injustice and will prove a veritable burden and an unwarranted hardship.

No other industry to-day renders the service in conservation and reclamation of woolen stock, for which there is such urgent need, as the cleaning and dyeing industry. This service has been completely recognized by the Government by its adoption of the dry-cleaning processes in reclaiming millions of pieces of uniforms for the War Department. It has further been recognized by the Government as a corrective and preventative factor in the matter of sanitation. These advantages so recognized officially are equally essential to and available for similar needs of the civilian population.

Without emphasis on the injustice of our position in the application of this tax, we believe that the revenue derived from this taxation for cleaning purposes would be more than offset by the resultant loss to conservation, which at this time should be urgently fostered rather than in any way discouraged.

Respectfully submitted.

ARTHUR BERG, *Chairman*,
C. G. HOWES, *Secretary*,
WAR SERVICE COMMITTEE,

Cleaning and Dyeing Industry of the United States.

INCOME, EXCESS PROFITS, AND WAR PROFITS TAXES.

The CHAIRMAN. Mr. Ben Watson is the next gentleman who desires to be heard. Mr. Watson, what interest do you represent?

STATEMENT OF MR. BENSON G. WATSON, REPRESENTING THE NATIONAL ASSOCIATION OF CREDIT MEN.

Mr. WATSON. I appear on behalf of the National Association of Credit Men, which is a business organization representing approximately 25,000 of the leading jobbers, manufacturers, and financial interests of the country; in fact, the largest organization of business units in the world.

Senator SMOOT. Where located?

Mr. WATSON. The headquarters are at 41 Park Row, New York.

The CHAIRMAN. To what section of the bill are you going to direct our attention?

Mr. WATSON. The purpose of my appearance is to point out some apparent inequalities, and to suggest some additional means of revenue which seems to have been overlooked.

Senator PENROSE. You represent the jobbers. In what particular line?

Mr. WATSON. Every line, every industry in the United States engaged in jobbing, manufacturing, or financial industries is a member of our association.

At the beginning of the present year, when the results of the present income tax law became apparent, the question of its effect upon credit granting became very important. The jobbing and manufacturing industries sell to retailers and distributors who are corporate, partnership, and individual.

Their situations, so far as capital stock or invested capital is concerned, and their volume of business, their probable income, in order to make credit granting safe and consistent, should be comparatively the same. We found, however, that under the law of 1917 there were very grave inequalities as the result of different forms of business organization. So that at the beginning of the year a committee was appointed, consisting of Mr. R. G. Elliott, chairman, of the Jaques

Manufacturing Co., of Chicago, Ill.; Mr. Charles D. Joyce, of the A. Colburn Co., of Philadelphia, Pa.; Mr. E. H. Jaynes, of the Cleveland Cliffs Iron Co., Cleveland, Ohio; Mr. W. M. Kennard, of Graupner, Love & Lamprecht, New York, N. Y., and Mr. S. J. Whitlock, of Belding Bros. & Co., of Chicago, Ill., with myself as counsel for the committee. We met on June 1 for our first formal meeting, and at that time prepared what we designated as a brief of the National Association of Credit Men, which was in turn submitted to all of the above 120 local associations in the various principal cities of the United States, in this way seeking to direct to the attention of the members of the Association the apparent inequalities and the recommendations and suggestions which we had, which we felt would equalize the burden. That brief was filed with the Ways and Means Committee, and I am pleased to say that some of the suggestions contained it have been recognized in the bill. In connection with this brief, and as a part of it, we included, at the end thereof, a graph showing the inequalities of the present law, taking seven distinct business conditions growing out of similar property holdings, invested capital, and distributive share to the individual. This graph shows clearly the inequalities, and the figures of the certified public inequalities, and the figures of the certified public accountant follow, and I desire to include that brief as a part of the suggestions which I will have to make before the committee.

The purpose of our work, which has continued since that time, has been to seek to equalize business organizations and business conditions subject to the tax, and to maintain what we call going values; that is, that the burden of the tax should not be so severe upon industry that it will curtail production, and thus limit income taxes and earning capacity in future years, and we have directed our attention to that in particular.

In going over the various matters which we had to suggest, there were two matters that came to our attention which we had not sought to find, but which we desire simply to suggest to the committee as being uncertainties in the proposed law which should be remedied. Section 213-B, page 9, is the provision which excepts as a deduction from gross incomes the proceeds of life insurance policies paid upon the death of the insured to individual beneficiaries, or to the estate of the insured. Section 233, page 35, provides that gross incomes of corporations shall be as defined in section 213.

The question that arose in our minds is as to whether or not insurance paid to the corporations is to be an allowable deduction. I am familiar with what the ruling has been under the present law, that is, that the excess of the amount paid over and above the premiums paid should be regarded as income. But I think there is an inconsistency in the law here which should be cured.

The other suggestion is in regard to the section following, the proceeds of life insurance policies paid upon the death of the insured to individual beneficiaries or to the estate of the insured; and the one following:

"The amount received by the insured as a return of premium or premiums paid by him under life insurance, endowment," etc. The question I wish to suggest, without commenting on it to the committee, is as to whether or not where endowment policies mature, which have been made payable to a beneficiary, and the amount of

the endowment policy is paid to an individual beneficiary, it is exempt under the law. I think the law is indistinct in that regard, and that should be remedied.

In other words, if your insurance is life, and you die, the amount paid your widow is exempted as income. If you have an endowment policy, and she is a beneficiary, at the maturity of the endowment it is paid to your wife; there is no provision for the exemption. I think it is clearly the intension that that should be done, and I think that ought to be remedied.

Senator THOMAS. This, I think, is a copy of the present law.

Mr. WATSON. Perhaps so; I am not sure.

Section 214-A (2), page 13, covers a deduction allowed to individuals, which is carried into the deductions allowed corporations. It provides:

All interest paid or accrued within the taxable year on indebtedness * * * in excess of interest received free from taxation under this title.

We believe that is a provision which will result not only inequitably, but will constitute a tax which is not intended. The law of 1917 permitted the deduction of the interest to the extent of capitalization on the rates selected or paid, equal to the capital stock plus one-half of the indebtedness. It has been suggested as being sound economy that the interest is a proper business expense, and I believe that is usually so conceded. If it is a proper business expense, and, under this law it can not be capitalized and added to invested capital, then the business entity should have the privilege of charging, as a business expense, the total amount of interest paid. That is our position from the business point of view.

The other is that by deducting tax free interest received, you are indirectly charging a tax upon municipals which you specifically exempt, and upon Liberty bonds. I think that position is clearly sound, and that that is the effect; that is, if one has a tax free interest coming from Liberty bonds, and is not entitled to take credit for all the interest paid, but must reduce the amount of the deduction by the amount of his tax free interest, he is indirectly paying a tax at the same rate on Liberty bonds.

Senator McCUMBER. And that is contrary to the agreement made, at least, when the first Liberty bonds were issued.

Mr. WATSON. Yes sir; and contrary to the expressed purpose of the bill.

Section 214, A-3, page 13, (a), (b), and (d) provide [reading]:

Taxes paid or accrued within the taxable year imposed (a) by the authority of the United States, except income, war-profits and excess-profits taxes; or (b) by the authority of any of its possessions, except the amount of income, war-profits and excess profits taxes allowed as a credit under section 222; or (d) in the case of a citizen or resident of the United States, by the authority of any foreign country, except the amount of income, war-profits and excess profits taxes, allowed as a credit under section 222.

The same exception is repeated at other places in the measure, and it is our belief that that is not a sound business principle, that the effect of it is to charge a tax upon the tax, which is not a recognized principle of taxation; that it has the effect of disturbing the ordinary methods used in business, and that all taxes are proper business charges against expenses, the same as all interest charges. I

recognize the fact that by changing that provision and going to what we consider a sound business principle it would release some of the tax which you will collect. Our answer to that is that if that is the case, the proper way to reach that tax is to readjust the rates.

Senator THOMAS. Concisely stated, your position is that there should be allowed deductions for all taxes paid?

Mr. WATSON. All taxes in the taxable year in which they accrue.

Senator McCUMBER. Because unless you do that, you are not taxing on your net profits, but you are taxing on a portion of your gross profits.

Mr. WATSON. Exactly so. Section 213-A, page 8, provides a definition for gross income, which I believe is the same as in the previous law, and the matter to which I desire to call your attention grows out of a very possible contingency which does not frequently occur, to one either preparing a tax law or one considering business policies. Under the definition of invested capital, as used in the previous acts, and as in this act, there is no permissible appreciation credit allowed to be added to invested capital. A conservatively managed business, having a property, which, according to its book accounts, is worth \$100,000, by reason of its appreciation, the cost of replacement, or the increased value of real estate in the neighborhood, becomes worth \$200,000. Being a conservative man, the business man insures to the amount of the appreciated value, either by co-insurance or a straight insurance plan, whichever may be selected, and has a fire. Assuming that it is a total loss, the insurance company pays to him \$200,000. His business accounting system only provides for that property as being worth \$100,000. The rulings have been to the effect that that is income. It is our contention that that item, if used in replacement, should not be counted as income.

If money is kept and used in other channels, it may be a proper item of income, and should be charged if the appreciation accrued since March, 1913. I shall not argue that. That may be correct and may be sound. But if the man is required to use the \$200,000 to replace the building consumed, he has no more after his building is completed than he had before. Nor is he entitled to add that \$200,000 to his invested capital, unless he pays the income tax on the increase in value.

There is a Treasury decision, No. 2706, which relates to war losses, which provides that where a loss is occasioned by reason of war times, or war destruction, and the building is replaced, the amount of the increase in value shall not be regarded as income; and provides, further, that if on account of business conditions the replacement can not be made immediately, the corporation or the individual may set up a replacement charge in his account of income retained for uses in his business, and he shall not be taxed on that account, within a given period, providing he gives bond and complies with other requirements of the Treasury Department.

It seems to me that provision should be embodied in the law, that where property consumed is compensated for by insurance, the increase over the book value of the property, if used in replacement, or if placed in a reserve for replacement, should not be treated as income, but proper safeguards should be thrown around the using of that sum for replacement when building conditions are normal.

Section 2, page 2, of our brief which was submitted contains the following recommendation:

Equality of the basis of the tax is essential so that the varying needs of the Government may be supplied by a change in the schedule of rates only, as frequent change of the basic principle of the law serves to cause disturbance to business and creates an unnecessary expense to the Government.

We, therefore, recommend that corporations, copartnerships, associations, and individuals engaged in business or trade be treated identically as to rates and exemptions.

Section 210, page 5, provides for the normal tax of 12 per cent on individuals.

Section 218-A, page 19, is the provision relating to partnership, which provides that partners shall report and pay the tax in their individual capacities only.

Section 230-A, page 31, provides a tax of 18 per cent on corporations, with a differential of 6 per cent for distributed profits.

It is our position and our contention that this is an income tax. It is not a privilege tax, not an excise tax, so far as these features of it are concerned. Corporations are creatures of the laws of the States in which they are incorporated or organized. They are not given or entitled to any Federal privilege other than that which is given to an individual or a partnership. The partnership is either the creature of the State in which it is organized, or it is contractual, and it likewise is not a creature of the Federal Government.

Before the lawmaking powers of the Federal Government a corporation, an association, a limited partnership, a partnership, and an individual engaged in business, stand upon identically the same basis, and are entitled to the same rights and privileges, and should not be penalized by reason of their being organized in one manner as against others organized differently.

Section 301, being the alternative war-profits and excess-profits tax provision, relates to corporations exclusively, and makes no provision for such taxes against an individual or a partnership. The proposed law is discriminatory against corporations, grossly so, in favor of individuals and partnerships, as the proposed draft is prepared. I do not ask you to accept the conclusions of the committee or the statements which I shall make, but I have had prepared by a certified public accountant, which I will submit as a part of the record, a tabulation containing the income, the taxes, the rate of tax, on capital, and the rate on income, of three different situations, one an individual in single proprietorship, having an invested capital of \$100,000, an income of \$25,000;

The second being an individual who, as one of three copartners owns a business of \$300,000, having in the prewar period a taxable income of \$30,000, having in the taxable year an income of \$75,000, one-third of which goes to the individual partner owing the same, making his capital invested \$100,000, and his income \$25,000;

The third being one of three owners of a corporation of \$300,000, having prewar earnings of \$30,000, having current earnings for the taxable year of \$75,000, which does not distribute any of its earnings made in the taxable year.

Another provision of the same kind for a corporation which distributes all of its earnings and another which distributes its earnings in excess of the amount of its taxes.

They are all identically the same, having the same invested capital and earnings.

The individual proprietor pays \$4,245 in income taxes and surtax.

The individual owner in the copartnership, having the same capital, has taxes of \$4,245.

The individual owner of one-third of the corporation not distributing its dividends pays \$13,564.

The individual owning one-third of the capital stock of a corporation the income of which is all distributed as dividends pays \$14,501.

The individual owning one-third of the capital stock, the income of which is all distributed with adjustments made for Federal income tax deductions so as not to tax at 18 per cent, that portion of income represented by the payment of income tax to the government, being the dropping out of the tax on the tax, \$13,469.44.

The individual owning one-third of the capital of a corporation, the income of which is all distributed as dividends except adjustment made for deduction of Federal taxes paid by corporations to arrive at residue available for distribution as dividends \$13,056.60.

The rate of taxation on the capital stock for the partner is 4.24 per cent; the individual, 4.24; the individual owner of the corporation is 13.5, and so on down the list. The tax on the income of the individual is 16.97 per cent, both for the sole proprietor and the partner. For the corporation it becomes a 54 per cent tax in one instance, and 58 in another, 53 in another, and 52 in another.

Senator THOMAS. Does that include the war-profits tax?

Mr. WATSON. Yes, figured on the basis of the alternative plan, either the war tax or excess profits, whichever is greater.

The comparison on the basis of \$100,000 invested capital and \$25,000 taxable year earnings was chosen for the reason that in our opinion that comes the nearest being the average case and would apply to a larger number of individuals and partnerships engaged in business or trade than any other amount which could be selected. The discrepancy would not be so large when the higher percentages of surtax are reached but there would be fewer instances to which the rule would apply.

There is no sound economic reason why this distinction should be made; for if a partnership or an individual is sufficiently large so that, if incorporated, it would be the subject of the excess profits or war profits tax, then by the very necessities of its business it will have a system of accounting to which the war profits and excess profits tax could be applied as well as a corporation, and the proper distinction between the business, as such, and the individual could be clearly drawn.

It is our contention that if it is the business entity which is to be made the subject of the tax all business entities or units regardless of the form of their organizations should be treated similarly.

Section 214A (11), page 16, provides for exempting contributions by individuals, but this provision is not made to extend to partnerships or corporations. The effect will be to reduce the income of the Red Cross and other relief organizations, for if corporations and partnerships are to be discriminated against in the matter of deductions and made to pay the tax upon their contributions they will obviously be curtailed.

Section 230A, page 31, provides for 6 per cent deduction for distributed earnings of corporations. It is our recommendation that in-

dividuals, partnerships and corporations should be treated alike, as to the exemptions, deductions, rates, and the war profits and excess profits taxes. Then a provision should be made to prevent the accumulation of unwarranted surplus accounts to prevent the payment of the surtax on dividends by the individual. It is our opinion that the plan for forcing distribution and providing for a tax on undistributed profits, provided for in the act of October 3, 1917, is preferable to the plan proposed in this act, as the plan in the proposed bill is in reality a tax upon capital increase which may be necessary for the reasonable requirements of the business.

Passing, now, to section 326, page 61 of the act, which is the provision which defines invested capital, it is our very firm conviction that the definition of invested capital is not sufficiently broad in that in paragraph A-3 it specifically excludes a large amount of sound capital assets. I mean by that the concluding paragraph, which provides [reading]:

And not including the increase in the value of any asset above the original cost until such increase is actually realized by sale.

The sixteenth amendment, which made possible the present proposed law, became effective March 1, 1913. It is our contention that on that date all assets, regardless of the question as to whether they were tangible or intangible, admissible or inadmissible, constituted invested capital of the citizen, corporation, or entity; that the invested capital was to be based upon that date. The proposed act makes it available for capital purposes when it has been the subject of purchase, but excludes it in the hands of the originating owner. That refers to so-called intangible property—good will, trade-marks, trade names, and property of that character. It very frequently happens that good will, developed in the hands of the original owner, is more valuable than it is when it is sold. It is actually sold, however, while yet in the hands of the original owner, whenever a share of the stock in the original corporation, or an interest in the partnership, is transferred to another owner, yet the corporation is not permitted to capitalize it.

If an organization develops the good will which makes its stock of \$100 a share par value worth \$300 a share the person who pays \$300 a share for that stock in the concern, having the good will, which has not been sold to it, is just as much and just as well entitled to have his investment protected as is the man who paid \$100 for a share of stock in a corporation having a par value of \$100 which corporation had purchased good will on the market. Our sole purpose is to equalize that provision, and it is our contention that good will, trade-marks, and trade names, having a determinable value, whether they have been sold or not, should be either permissible invested capital items to the corporation which originated them, or the corporation which purchases those intangibles on the market should not be entitled to them. We do not care which way you go.

The proposition is recognized in this law, because, in section 201, page 4, we find the provision:

That for the purpose of ascertaining the gain derived or loss sustained from the sale or other disposition of property, real, personal, or mixed, the basis shall be—

(a) In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and

(b) In the case of property acquired on or after that date, (1) the cost thereof, or (2) the inventory value.

It is our contention that that provision in this act recognizes the fact that property, regardless of its ownership, regardless of its transfer, regardless of its character, if it had a value on March 1, 1913, is recognized as invested capital.

Senator THOMAS. Has not a good deal of this intangible wealth of which you speak been converted into capital stock?

Mr. WATSON. I think there has been an attempt to do that in many quarters. On the other hand, practically every soundly managed business concern that is closely held has not done so, and could not do so under the law, because in order to do so they must transfer the ownership to somebody else. They can not retain 50 per cent of the ownership themselves and increase the capitalization under the present law, and this fact creates an obvious inequality.

The proposition is recognized in another place in this bill, where you provide for the basis of the capital-stock tax. There you provide, first, that you must submit your assets and liabilities; second, the market price of your stock; third, your average income for the five previous years, for capitalization purposes, and that the capital-stock tax is based on whichever is highest.

The principle has also been recognized by judicial decision, in the Big Four case, to the effect that the change of situation after the adoption of the law can not be taken advantage of to change the basis of tax.

Our recommendation on page 2, section 3, of our brief contains the following [reading]:

We believe that so far as possible all classes of citizens and residents should bear a part of the expense of winning the war.

We, therefore, recommend that personal exemptions remain as at present, but that a flat individual income tax not to exceed \$5 be assessed against all individuals whose income equals or exceeds \$800, this to be in addition to whatever taxes are now or hereafter levied, and to be collected and paid at the source wherever possible.

In the proposed bill reporting at the source has been increased from \$800 to \$1,000. We very graciously accept that change, and suggest that the provision which we recommend apply to that provision, because the thought of the law was suggested by the seeming uselessness of reporting the amount of income less than the amount of exemption which was required by the old law.

The present requirement of reporting \$1,000 when \$1,000 is the minimum exemption, and the amount at which the tax begins contains a great deal more in its favor. But the thing we had in mind in recommending this tax is twofold. In the first place, we estimate that there are 30,000,000 people in the United States earning \$1,000, and that a tax of \$5 will produce \$150,000,000.

If, however, you pass to section 1001, page 144 of the act, you will find a provision of the law which in some respects closely resembles our recommendation, except that it is made to apply to all persons who are proprietors of any trade, business, or profession, and having an income exceeding \$2,000, the tax to be \$10, with the provision, however, that it should not apply to certain specified classifications.

Senator THOMAS. To agriculture.

Mr. WATSON. Yes, sir; and we seriously object to the exemption of anyone. We are of the opinion that it is vitally important for

the interests of the country to bring home to every citizen, every person, every individual, that fact that he or she has some part in the Government's plan of financing the war. We believe it is not only the duty of everyone having an income of \$1,000 to pay something directly, whether he is subject to an income tax or not, but we believe it is a privilege which should be extended to him. We believe it will produce considerable revenue which will be easily collectible. Our suggestion is that wherever possible the tax be collected and paid at the source, and as a workable means of affecting this purpose we suggest that the tax be collected by the employer and deducted from the earnings of every employee whose rate of wage equals \$1,000 a year, deduction to be made upon a definite date to be fixed by the act at the date as shown by the statistical bureau as being the one upon which most people are employed; that it also be included as a part of the fixed tax of every one required to make a tax return under the present law, but deductible from the individual's tax if paid by his employer; that an affidavit be required from all others who are employed upon the date fixed, or who are not required to make the individual income tax return by reason of existing exemptions, stating whether or not their earnings equal the sum of \$1,000 per year, and if so, the tax shall be collectible. This plan would seem to have the effect of reaching all classes of employees and citizens whose earnings or rate of earnings equal \$1,000 per year, and without imposing an undue expense in the collection.

The provision has been submitted to a large number of people throughout the country, and as reflecting the manner in which it has been received I have here a letter signed by various business men in Indianapolis, Ind., which I would like to read to the committee. It is as follows [reading]:

INDIANAPOLIS ASSOCIATION OF CREDIT MEN,
Indianapolis, Ind., August 28, 1918.

We are strongly in favor of a flat individual income tax of not exceeding \$5, believing that it is a wise policy that permits many individuals, who now have no opportunity of doing so, the privilege of having a more personal interest in the carrying on of the war by means of payment of this direct tax. The majority of the committee were in favor of a minimum income of \$1,000 against which to base this tax, believing that individuals having an income of less than that amount would on account of the high cost of living find a direct flat tax somewhat of a hardship, although it was conceded that there are individuals without dependents receiving incomes of less than \$1,000, who not only could pay such flat tax, but would be perfectly willing to; in fact, would feel that an injustice was being done by refusing to permit them to furnish this part of the sinews for carrying the war to a successful conclusion.

I thank you very much for your attention, and shall be pleased to answer any inquiries or to submit any further statements you may desire.

Senator TOWNSEND. Did I understand you had revised this brief you have filed in the House?

Mr. WATSON. This brief was prepared before any bill was introduced in the House. We have not changed our position from the position laid down in the brief.

Senator ROBINSON. Some of the suggestions in the brief have already been incorporated in the bill?

Mr. WATSON. Yes, sir.

Senator ROBINSON. I think you ought to indicate on the brief, or in connection with your statement, what suggestions have been incorporated. You can do that at your leisure.

Senator PENROSE. Mark the paragraphs that are incorporated in the bill, so that they may be indicated when the hearing is printed.

(The document referred to by Mr. Watson is here printed in full, as follows:)

BRIEF OF THE NATIONAL ASSOCIATION OF CREDIT MEN.

[Prepared by R. G. Elliott, chairman, Jaques Manufacturing Co., Chicago, Ill.; Charles D. Joyce, the A. Colburn Co., Philadelphia, Pa.; E. H. Jaynes, Cleveland-Cliffs Iron Co., Cleveland, Ohio; W. M. Kennard, Graupner, Love & Lamprecht, New York, N. Y.; S. J. Whitlock, Belding Bros. & Co., Chicago, Ill.; and B. G. Watson, counsel, Watson, Stouffer, Davis & Gearheart, Columbus, Ohio.]

I.

The National Association of Credit Men, comprising 24,636 of the leading manufacturers, jobbers, and financial institutions of the United States, and being the largest organization of commercial units in the world, fully recognizes its obligations to the Government and pledges its fullest support to the winning of the war.

The Government organization of its war activities now progressing so splendidly places upon organized business the fullest responsibility of furnishing increasing financial support.

Fully recognizing the inadequacy of existing measures for the production of sufficient revenues for the Government's expanding operations, we have nevertheless had constantly before us the fact that future requirements must inevitably be still greater and that productive industry must furnish the principal source from which the Government secures its revenues, we therefore, tender our fullest support and cooperation to the end that an economically sound and equitable basis for future taxation be laid in the measures now under consideration.

From an exhaustive study of the present income and excess profits tax laws, we find that the operation and results of the same are inequitable, and in many instances, impose unwarranted hardships, and in others correspondingly unwarranted exemptions, which in the aggregate do not result in producing maximum revenues with minimum disturbance to the source of revenue. To illustrate the character of the inequalities, we have caused to be prepared and appended hereto a compilation of a variety of conditions taken from actual business operations which show the effect of the law, not only upon the entity but upon the constituent holders thereof. These inequalities arise largely from the different manner in which different forms of business operations are treated by the law and the varying sources from which taxable income is derived. In arriving at the conclusions and recommendations hereinafter set out, we have had in mind, the equal encouragement of productive industry to the end that not only more current revenue may be obtained from income but that the sources of future taxable income may remain undisturbed.

II.

Equality of the basis of the tax is essential so that the varying needs of the Government may be supplied by a change in the schedule of rates only, as frequent change of the basic principle of the law serves to cause disturbance to business and creates an unnecessary expense to the Government.

We therefore recommend that corporations, copartnerships, associations, and individuals engaged in business or trade be treated identically as to rates and exemptions.

III.

We believe that so far as possible all classes of citizens and residents should bear a part of the expense of winning the war.

We therefore recommend that personal exemptions remain as at present, but that a flat individual income tax not to exceed \$5 be assessed against all individuals whose income equals or exceeds \$800, this to be in addition to

whatever taxes are now or hereafter levied, and to be collected and paid at the source wherever possible.

IV.

It is the duty of every citizen, resident, corporation, copartnership, or association to contribute in equal proportion to his or its ability to pay from his or its normal income.

We therefore recommend that the normal rate be increased to not to exceed 8 per cent, and that the surtax be continued. It would seem that incomes under \$100,000 could be fairly expected to bear a relatively higher rate of surtax than they at present bear, while at the same time the entire schedule might be materially increased.

V.

Double taxation should be avoided.

We therefore recommend that corporate, copartnership, and association earnings in the hands of individuals be exempt from taxation to the extent of the normal tax paid by the corporation, copartnership, or association on their earnings.

We further recommend that income taxes assessed be an allowable deduction from gross income for the year in which they accrue.

VI.

We believe that so-called unearned incomes should be taxed on the same basis as earned incomes.

VII.

The war relief activities are calling largely upon corporations for assistance; we therefore recommend that contributions by corporations made to strictly war relief organizations be an allowable deduction from gross income.

VIII.

We believe that there is no sound economic relation between invested capital and income, and that an excess profits law based thereon penalizes conservative business management and personal effort, and places a premium on over capitalization and loose management and can not be equitably assessed.

We therefore recommend that an excess profits tax be formulated by the terms of which the trade or business be allowed an earning equivalent to its prewar earnings before an excess tax is levied. A business or trade not in existence during the prewar period or with subnormal earnings therein should have the average earning of the industry for the prewar period in its line; that after the exemption of its prewar earnings a substantial graduated increasing rate should be assessed, based on a percentage increase over prewar earnings. This tax to be levied on all corporations, copartnerships, associations, and individuals engaged in "trade or business," which last terms of "trade" or "business" shall not include professions or personal service.

IX.

We recommend that undistributed earnings of a copartnership should be treated the same as the undistributed earnings of a corporation, including a 10 per cent tax on undistributed earnings not necessary for the reasonable requirements of the business.

X.

In the event that the law is to be based on the relation of invested capital to income, then provision should be made whereby good will, trade names, patents, or other intangible property having a determinable value should be placed on the same basis, whether produced by the present owner or paid for in cash or tangible property.

And further, that in arriving at the amount of invested capital, due regard should be given to the market value or earning value of the stock or shares as well as to the average amount of borrowed money customarily employed in the business.

The foregoing provisions are each vitally important in order to maintain the market value and avoid unnecessary shrinkage of security in the hands of small investors who are to a greater or less degree dependent thereon for their personal income.

XI.

In order that an unnecessary drain upon the financial resources of the country may be avoided at tax paying periods, we recommend that the same be payable one-third on June 15, one-third on July 15, and one-third on August 15 of each year, and that anticipation certificates of indebtedness be available throughout the year.

XII.

We suggest that in the framing of the present revenue measure due consideration be given to the fact that since the conclusion of the prewar period a large number of industries have been organized, many of which do not have a parallel in the prewar period by which to measure its adequate prewar earnings; in others of which the operations have been conducted upon individual responsibility of its officers who are affiliated with other kindred industries, and in which, by reason of the requirements of the business a large capital during the year, as a whole, is not necessary and whose earnings are so disproportioned to its capital requirements as to render a comparison with similar lines during the prewar period impossible without an injustice to the principals engaged.

XIII.

In formulating the foregoing suggestions and recommendations we have had constantly in mind the fact that, while organized business will produce the larger part of the earnings from which the Government must obtain its revenue, yet these units, either corporate, copartnership, or association, comprise a large number of individual partners or shareholders who rely for their source of income upon the earnings of the larger units.

We believe that the embodiment of our suggestions and recommendations in a revenue measure will have the effect of placing the ultimate burden of the tax upon the individuals in whose hands only the income is liquid and available for tax purposes, on an equitable basis of income and ability to pay.

CHICAGO, May 21, 1918.

We have compiled the following statements in order to show the variation in amounts and percentages of the tax on the same amount of income derived from investment under varying conditions or received without investment as salary.

Yours, respectfully,

WM. W. THOMPSON & Co.,
Certified Public Accountants.

SUMMARY.

Taxes on investments and incomes under following conditions would be as shown below:

AMOUNT AND PER CENT ON CAPITAL INVESTED.

Condition.	A.		B.		C.		D.	
	Amount.	Per cent.	Amount.	Per cent.	Amount.	Per cent.	Amount.	Per cent.
1. Capital invested on corporation at three times par.....	\$8,586.92	5.72	\$5,067.62	5.63	\$1,674.36	5.58	\$837.18	5.58
2. Capital invested in reorganized corporation, which has bought good will, etc., for cash.....	3,488.11	2.23	1,934.03	2.15	602.76	2.01	301.38	2.01
3. Capital invested in reorganized corporation which bought good will, etc., for stock.....	5,883.26	11.76	3,401.37	11.31	1,107.00	11.07	553.50	11.07
4. Capital invested in single proprietorship.....	2,008.00	1.34	610.00	.68	60.00	.20	5.00	.10
5. Capital invested in partnership.....	8,215.40	5.48	4,761.16	5.29	1,506.24	5.02	744.00	4.96
6. Capital, none; entire income from salary.....	2,641.60	.....	1,182.00	.....	60.00	.....	5.00	.....
7. Capital invested in bonds.....	1,480.00	.986	610.00	.677	60.00	.20	5.00	.022

AMOUNT AND PER CENT ON EARNINGS OF INVESTMENTS.

1. Capital invested on corporation at three times par.....	\$8,586.92	38.16	\$5,067.62	37.54	\$1,674.36	37.20	\$837.18	37.20
2. Capital invested in reorganized corporation which has bought good will, etc., for cash.....	3,488.11	15.50	1,934.03	14.32	602.76	13.39	301.38	13.39
3. Capital invested in reorganized corporation which bought good will, etc., for stock.....	5,883.25	26.15	3,401.37	25.20	1,107.00	26.00	553.50	25.00
4. Capital invested in single proprietorship.....	2,008.00	8.92	610.00	4.52	60.00	1.33	5.00	.22
5. Capital invested in partnership.....	8,215.40	36.52	4,761.16	35.27	1,508.24	33.51	744.00	33.06
6. Capital, none; entire income from salary.....	2,641.00	11.74	1,162.00	8.61	60.00	1.33	5.00	.22
7. Capital invested in bonds.....	1,480.00	6.57	610.00	4.52	60.00	1.33	5.00	.22

Condition No. 1.—Smith & Co. is a corporation organized in 1900, with a capital stock of 10,000 shares of a par value of \$100 per share; total par value, \$1,000,000. The market value of this stock, measured by sales for past five years, has been \$300 per share; total market value, \$3,000,000.

The earnings on the above stock for past seven years has been an average of \$45 per share, which is equal to 45 per cent on par or 15 per cent on market value.

The stock is all outstanding and was purchased at \$300 per share by individuals who are married but without children; and the income from this stock constitutes their entire income.

After computing the Federal taxes and deducting same from net profits, all the balance of net income was distributed as dividends to stockholders.

Under the above conditions the taxes and rate per cent of income and rate per cent of investment are as shown below:

Stockholder.	No. of shares.	Actual capital invested.	Earnings of investment.	Share of corporation taxes.	Balance of earnings received as dividends.	Personal taxes.	Total corporation and personal taxes.	Per cent of taxes on—	
								Capital invested.	Earnings of investment.
A.....	500	\$150,000.00	\$22,500.00	\$8,371.80	\$14,128.20	\$214.12	\$8,586.92	5.72	38.16
B.....	300	90,000.00	13,500.00	5,023.08	8,476.92	44.54	5,067.62	5.63	37.54
C.....	100	30,000.00	4,500.00	1,674.36	2,825.64	None.	1,674.36	5.58	37.20
D.....	50	15,000.00	2,250.00	837.18	1,412.82	None.	837.18	5.58	37.20
Others.....	9,050	2,715,000.00	407,250.00	151,529.58	255,720.42	Var.	.....	Var.	.....
	10,000	3,000,000.00	450,000.00	167,436.00	282,564.00	.....	.....	.....	.....

Condition No. 2.—Jones & Co. is a corporation organized in 1900 in same business and with same capital as Smith & Co., but in 1912 reorganized; a new corporation taking over the business and paying in cash \$2,000,000 for the good will, trade-marks, and trade brands of Smith & Co. and \$1,000,000 for the net tangible assets; making the total invested capital of the new company \$3,000,000.

Otherwise the conditions are the same as Smith & Co. stated above.

The taxes and rate per cent of income and rate per cent of investment under condition No. 2 are as shown below:

Stockholder.	Number of shares.	Actual capital invested.	Earnings of investment.	Share of corporation taxes.	Balance of earnings received as dividends.	Personal taxes.	Total corporation and personal taxes.	Per cent of taxes on—	
								Capital invested.	Earnings of investment.
A.....	1,500	\$150,000.00	\$22,500.00	\$3,013.80	\$19,486.20	\$474.31	\$3,488.11	2.33	15.50
B.....	900	90,000.00	13,500.00	1,808.28	11,691.72	125.75	1,934.03	2.15	14.32
C.....	300	30,000.00	4,500.00	602.76	3,897.24	None.	602.76	2.01	13.39
D.....	150	15,000.00	2,250.00	301.38	1,948.62	None.	301.38	2.01	13.39
Others.....	27,150	2,715,000.00	407,250.00	54,549.78	352,700.22	Var.	.....	Var.	.....
Total..	30,000	3,000,000.00	450,000.00	60,276.00	399,724.00	.....	.....	.....	.....

Condition No. 3.—Assume that all particulars under condition No. 2 are the same under this caption except that \$2,000,000 stock was issued for good will, trade-marks and trade brands instead of cash paid for same. Then in that event the \$2,000,000 good will, etc., can only be valued for purpose of determining the invested capital at 20 per cent of outstanding stock, or \$800,000, thus making the total invested capital of company \$1,600,000.

The taxes and rate per cent of income and rate per cent on investment under condition No. 3 is as follows:

Stockholder.	Number of shares.	Actual capital invested.	Earnings of investment.	Share of corporation taxes.	Balance of earnings received as dividends.	Personal taxes.	Total corporation and personal taxes.	Per cent of taxes on—	
								Capital invested.	Earnings of investment.
A.....	1,500	\$50,000.00	\$22,500.00	\$5,535.00	\$16,965.00	\$348.25	\$5,893.25	11.76	26.15
B.....	900	30,000.00	13,500.00	3,321.00	10,179.00	80.37	3,401.37	11.31	25.20
C.....	300	10,000.00	4,500.00	1,107.00	3,393.00	None.	1,107.00	11.07	25.00
D.....	150	5,000.00	2,250.00	553.50	1,696.50	None.	553.50	11.07	25.00
Others.....	27,150	905,000.00	407,250.00	100,237.50	307,012.50	Var.	.....	Var.	.....
Total....	30,000	1,000,000.00	450,000.00	110,754.00	339,246.00	.....	.....	.....	.....

Condition No. 4.—If there were no corporation taxes and the stockholders under condition No. 1 received all of their pro rata of earnings of the corporation without any tax deduction, which in effect would put each stockholder in the position of a single proprietor, then the taxes and rate per cent of income and rate per cent on invested capital would be as follows:

Proprietors.	Number of shares.	Actual capital invested.	Earnings of investment.	Individual taxes.			Per cent of taxes on—	
				Excess-profits tax.	Income tax.	Total taxes.	Capital invested.	Earnings of investment.
A.....	500	\$150,000.00	\$22,500.00	\$600.00	\$1,408.00	\$2,008.00	1.34	8.92
B.....	300	90,000.00	13,500.00	None.	610.00	610.00	.68	4.42
C.....	100	30,000.00	4,500.00	None.	60.00	60.00	.20	1.33
D.....	50	15,000.00	2,250.00	None.	5.00	5.00	.10	.22

Condition No. 5.—If the proposition as stated in condition 1 was treated as a partnership the results would be as follows:

Partners.	Number of shares.	Actual capital invested.	Earnings of investment.	Excess profits.	Individual income tax.	Total taxes.	Per cent of taxes on—	
							Capital invested.	Earnings of investment.
A.....	500	\$150,000.00	\$22,500.00	\$7,440.00	\$775.40	\$8,215.40	5.48	36.52
B.....	300	90,000.00	13,500.00	4,464.00	267.16	4,731.16	5.23	35.27
C.....	100	30,000.00	4,500.00	1,488.00	21.24	1,509.24	5.02	33.43
D.....	50	15,000.00	2,250.00	744.00	None.	744.00	4.96	31.06

Condition No. 6.—If the stockholders of Smith & Co. had not invested their money in that company, but received salaries of a like amount as the earnings of the stock of the stockholders of Smith & Co., then the tax on their income would be as follows:

Employees.	Actual capital invested.	Salary received.	Individual income tax.	Per cent of taxes on—	
				Capital invested.	Earnings of investment.
A.....	None.	\$22,500.00	\$2,641.60	None.	11.74
B.....	None.	13,500.00	1,182.00	None.	8.61
C.....	None.	4,500.00	60.00	None.	1.33
D.....	None.	2,250.00	5.00	None.	.22

Condition No. 7.—If income of Smith & Co. stockholders had all been derived from bond interest:

Bond holders.	Actual investment.	Earnings of investment.	Individual taxes.	Per cent of taxes on—	
				Capital invested.	Earnings of investment.
A.....	\$150,000.00	\$22,500.00	\$1,480.00	0.986	6.57
B.....	90,000.00	13,500.00	610.00	.677	4.52
C.....	30,000.00	4,500.00	60.00	.200	1.33
D.....	15,000.00	2,250.00	5.00	.033	.22

TAX ANALYSIS FOR NATIONAL ASSOCIATION OF CREDIT MEN.

THE NATIONAL ASSOCIATION OF CREDIT MEN,
Chicago, Ill.

GENTLEMEN: We have compiled the following statements in order to show the effect of the combined income and excess profits or war profits taxes, as proposed in House bill No. 12863, on the income of an individual with an investment in any one of the four following different business organizations:

- (a) Single proprietorship.
- (b) Copartnership.
- (c) Corporation not distributing its income as dividends.
- (d) Corporation distributing all its income as dividends.

We show the amount of taxes in each case as well as the rate per cent of the taxes based on both the invested capital as well as on the income.

You will note that with identically the same investment and identically the same income the amount of tax varies from \$4,245 against an individual engaged in business as a single proprietor or as a partner in a copartnership to \$13,564 against an individual with his money invested in a corporation, which does not distribute its income as dividends, and to \$14,501 against an individual with his money invested in a corporation which distributes all its income as dividends. The percentages also vary from 4.245 per cent to 14.501 per cent on capital invested; and on income from 16.97 per cent to 58 per cent.

The amount of tax and the relative percentages in class C will be increased if and when the corporation does declare dividends providing this action takes place during a year in which the tax laws are in force. The increase will depend entirely on the tax rates in force at that time.

We have compiled Exhibits C and D in strict accordance with the text of the House bill as it now stands, but call attention to the wording of paragraph (a) of section 230, page 14, which is as follows:

"In the case of a domestic corporation 18 per centum of the amount of the net income in excess of the credits provided in section 236: *Provided*, That the rate shall be 12 per centum upon so much of this amount as does not exceed the sum of (1) the amount of dividends paid during the taxable year, plus (2) the amount paid during the taxable year out of earnings or profits in discharge of bonds and other interest-bearing obligations outstanding prior to the beginning of the taxable year."

This paragraph should be changed so as to give the taxpayer the benefit of the 12 per cent rate on that portion of the corporate net income used to pay the Federal income tax with, as it is obvious that while a corporation may pay out all its net income for a single year in dividends and treat its taxes as being paid out of succeeding years' income it can not continue this process indefinitely. We have prepared Exhibit E to give expression to an anticipated change in paragraph (a), section 230, which will give the taxpayer the right to compute the tax on income used in paying income tax with at the 12 per cent rate instead of the 18 per cent rate as now called for in House bill.

We have also prepared Exhibit F to give expression to the amount of dividends available for distribution, as it is clear that a corporation can not continually distribute all its net income as dividends. It must pay the Federal taxes (which are not allowed as an expense of the business) and the residue is the only amount available for dividends.

If the present bill H. R. 12863 becomes a law it will penalize those individuals who are engaged in business under a corporate form, and will place them at a serious disadvantage over those engaged in business as single proprietors or in copartnerships and it is to show this variation in taxes that we submit the following summary supported by exhibits and schedules, showing the details by which the summary is made up.

Respectfully submitted.

WM. W. THOMPSON & Co.,
Certified Public Accountants.

COMPARATIVE SUMMARY.

	Capital invested.	Income.	Taxes.	Rate of tax.	
				On capital.	On income.
A. Individual in single proprietorship.....	\$100,000.00	\$25,000.00	\$4,245.00	<i>Per cent.</i> 4.245	<i>Per cent.</i> 16.97
B. Individual as one of 3 copartners.....	100,000.00	25,000.00	4,245.00	4.245	16.97
C. Individual owning one-third of capital of corporation the income of which is not distributed as dividends.....	100,000.00	25,000.00	13,564.00	13.564	54.25
D. Individual owning one-third of capital of corporation the income of which is all distributed as dividends.....	100,000.00	25,000.00	14,501.00	14.501	58.00
E. Same as C except adjustment made for Federal income tax deduction so as not to tax at 18 per cent, that portion of income represented by payment of income tax to Government.....	100,000.00	25,000.00	13,469.44	13.469	53.99
F. Same as D except adjustment made for deduction of Federal income taxes paid by corporation to arrive at residue available for distribution as dividends.....	100,000.00	25,000.00	13,056.68	13.057	52.23

EXHIBIT A.

Computation of tax on income of an individual citizen or resident of the United States whose invested capital in trade is \$100,000, and income is \$25,000.

Normal tax:	Tax.	
Net income	\$25,000	
Less personal exemption	2,000	
Net taxable income.....	23,000	
Taxable at 6 per cent.....	4,000	\$240
Taxable at 12 per cent.....	19,000	2,280
Total normal tax		<u>2,520</u>

Surtax:	
Net income.....	\$25,000
Less exemption.....	5,000
Net taxable income.....	20,000
2 per cent on \$7,500—\$5,000=\$2,500.....	\$50
3 per cent on \$10,000—\$7,500=\$2,500.....	75
7 per cent on \$15,000—\$10,000=\$5,000.....	350
10 per cent on \$20,000—\$15,000=\$5,000.....	500
15 per cent on excess over \$20,000=\$5,000.....	750
Total surtax.....	1,725
Total normal and surtax.....	4,245
(Not subject to excess profits or war profits tax.)	

EXHIBIT B.

Computation of tax on income of one of three members of a domestic co-partnership whose invested capital in trade is \$300,000, and income is \$75,000.

Normal tax:		Tax.
Net income.....	\$25,000	
Less personal exemption.....	2,000	
Net taxable income.....	23,000	
Taxable at 6 per cent.....	4,000	\$240
Taxable at 12 per cent.....	19,000	2,280
Total normal tax.....		2,520
Surtax:		
Net income.....	25,000	
Less exemption.....	5,000	
Net taxable income.....	20,000	
2 per cent on \$7,500—\$5,000=\$2,500.....		50
3 per cent on \$10,000—\$7,500=\$2,500.....		75
7 per cent on \$15,000—\$10,000=\$5,000.....		350
10 per cent on \$20,000—\$15,000=\$5,000.....		500
15 per cent on excess over \$20,000=\$5,000.....		750
Total surtax.....		1,725
Total normal and surtax.....		4,245
(Not subject to excess profits or war profits tax.)		

EXHIBIT C.

Computation of tax on income of 1 of a total of 3 equal stockholders owning all the stock of a domestic corporation whose invested capital in trade is \$300,000 and income is \$75,000, none of which income distributed as dividends.

CORPORATION TAX COMPUTED.

Normal tax:		Tax.
Net income.....	\$75,000	
Less—		
War profits tax.....	\$33,600	
Specific exemption.....	2,000	
	35,600	
Subject to 18 per cent tax.....	39,400	\$7,092
War profits tax, computed as per schedule No. 1.....		33,600
Total corporation tax.....		40,692

INDIVIDUAL TAX COMPUTED.

[No dividends received.]

Normal tax: One-third of the above tax paid indirectly by individual through corporation. There is in this case no tax direct on the individual. The tax paid by corporation for account of the individuals was----- \$13, 564

EXHIBIT D.

Computation of tax on income of 1 of a total of 3 equal stockholders owning all the stock of a domestic corporation whose invested capital in trade is \$300,000 and income is \$75,000, all of its income being distributed as dividends.

CORPORATION TAX COMPUTED.

[All income distributed as dividends.]

		Tax.
Normal tax:		
Net income-----	\$75, 000	
Less—		
War profits tax-----	\$33, 600	
Specific exemption-----	2, 000	
	<u>35, 600</u>	
Subject to 12 per cent tax-----	39, 400	\$4, 728
War profits tax, computed as per schedule No. 1-----		<u>33, 600</u>
Total corporation taxes-----		<u>38, 328</u>

INDIVIDUAL TAX COMPUTED.

[Entire corporate earnings received as dividends.]

Normal tax: None on dividends.

Surtax:

Net income from dividends-----	\$25, 000	
Less exemption of-----	5, 000	
Net taxable income-----	<u>20, 000</u>	
2 per cent on \$7,500—\$5,000=\$2,500-----		\$50
3 per cent on \$10,000—\$7,500=\$2,500-----		75
7 per cent on \$15,000—\$10,000=\$5,000-----		350
10 per cent on \$20,000—\$15,000=\$5,000-----		500
15 per cent on excess over \$20,000=\$5,000-----		<u>750</u>
Total surtax-----		<u>1, 725</u>
Add individual's share of tax paid by corporation in his behalf as per above, being one-third of \$38,328-----		<u>12, 778</u>
Total taxes paid direct by individual and indirectly through the corporation-----		<u>14, 501</u>

EXHIBIT E.

Computation of tax on income of 1 of a total of 3 equal stockholders owning all the stock of a domestic corporation whose invested capital in trade is \$300,000 and income is \$75,000. None of which income is distributed as dividends.

CORPORATION TAX COMPUTED.

No dividends paid.

Normal tax:			Tax.
Net income	\$75,000.00		
Less—			
War-profits tax (see schedule No. 1)	\$33,600.00		
Specific exemption	2,000.00		
	<u>35,600.00</u>		
Subject to 12 per cent tax	39,400.00	\$4,728.00	
Less normal taxes	<u>4,728.00</u>		
Subject to additional tax of 6 per cent on account of not being distributed	34,672.00	2,080.32	
War-profits tax, computed as per schedule No. 1		<u>33,600.00</u>	
Total		<u>40,408.32</u>	

INDIVIDUAL TAX COMPUTED.

[No dividends received.]

Normal tax: One-third of the above tax paid indirectly by individual through corporation

\$13,469.44

EXHIBIT F.

Computation of tax on income of 1 or a total of 3 equal stockholders owning all the stock of a domestic corporation whose invested capital in trade is \$300,000 and income is \$75,000, all of its residue of income, after paying Federal taxes, being distributed as dividends.

CORPORATION TAX COMPUTED.

[All income, after paying taxes, distributed as dividends.]

			Tax.
Normal tax:			
Net income	\$75,000.00		
Less—			
War-profits tax (schedule No. 1)	\$33,600.00		
Special exemption	2,000.00		
	<u>35,600.00</u>		
Subject to 12 per cent tax	39,400.00	\$4,728.00	
War-profits tax, computed as per schedule No. 1		<u>33,600.00</u>	
Total corporation taxes		<u>38,328.00</u>	

INDIVIDUAL TAX COMPUTED.

[Entire corporate earnings, less taxes paid, received as dividends.]

Normal tax: None on dividends.

Surtax:

Net income from dividends—

One-third net income of \$75,000..... \$25,000.00

Less corporation taxes paid..... 12,776.00

Dividends received..... 12,224.00

Less exemption of..... 5,000.00

Net income subject to surtax..... 7,224.00

2 per cent on \$7,500—\$5,000=\$2,500..... \$50.00

3 per cent on \$10,000—\$7,500=\$2,500..... 75.00

7 per cent on excess over \$10,000=\$2,224..... 155.68

Total surtax..... 280.68

Add individual's share of tax paid by corporation in his behalf
as per above, being one-third of \$38,328..... 12,776.00Total taxes paid direct by individual and indirectly
through the corporation..... 13,056.68*Schedule No. 1.*—War-profits and excess-profits tax computations supporting
Exhibit "C".

WAR-PROFITS METHOD.

Net income..... \$75,000.00

Less—

Specific exemption..... \$3,000.00

10 per cent prewar profits..... 30,000.00

33,000.00

Income taxable at 80 per cent..... \$42,000.00

Total war-profits tax 80 per cent of \$42,000, equal..... \$33,600.00

EXCESS PROFITS METHOD.

Net income..... \$75,000.00

Less—

Specific exemption..... \$3,000.00

8 per cent invested capital..... 24,000.00

27,000.00

Income taxable as below..... 48,000.00

15 per cent of invested capital..... \$45,000.00

Less exemptions..... 27,000.00

Taxable at 35 per cent..... 18,000.00

Tax.
6,300.00

20 per cent of invested capital..... 60,000.00

Less 15 per cent of capital..... 45,000.00

Taxable at 50 per cent..... 15,000.00

7,500.00

Excess of income over 20 per cent of invested capital
taxable at 70 per cent..... 15,000.00

10,500.00

Total taxable income..... 48,000.00

Total excess-profits tax..... \$24,300.00

NOTE.—Inasmuch as the war-profits method gives a larger tax than the excess-profits method it is the tax to use in computing the income tax return and amounts to \$33,600.

Conforming to the request of Senators Penrose and Robinson that we indicate the principles in the brief which have been embodied in the proposed law, we suggest that they are as follows:

First. In paragraph 2 the basic exemption and tax rate on income as between individuals, partnerships, and incorporations.

Second. In paragraph 4, our recommendation, "it would seem that incomes under \$100,000 would be fairly expected to bear a relatively higher rate of surtax."

Third. In paragraph 5, recommending the exemption of dividends to the amount of the normal tax paid by the entity.

Fourth. Paragraph 6.

Fifth. Paragraph 8, suggesting the prewar earnings as the basis of the exemption, has been recognized in the war-profits tax.

Sixth. Paragraph 11, recommending the payment of the tax in installments, has been adopted with modifications as to dates.

Seventh. Paragraph 12, the lower maximum rates provided for smaller corporations and a provision for a proper exemption to entities for subnormal earnings during the prewar period has been provided for.

During the hearing, but too late to be presented in the argument, the following telegram was received from a prominent member of the association:

"Urge * * * that if invested capital is reduced by dividends paid during current year, current earnings should be an addition to invested capital. Consistency is a virtue which should not be overlooked."

(The following letter was subsequently received, and, by order of the chairman, is here printed in full, as follows:)

EXCESS-PROFIT TAX AS IT AFFECTS MODERATE-SIZED CORPORATIONS ENGAGED IN A HAZARDOUS FORM OF BUSINESS.

BUFFALO, N. Y., September 17, 1918.

Hon. F. M. SIMMONS,

Senate Finance Committee, Washington, D. C.

DEAR SIR: The excess-profit tax bears most heavily on small or medium-sized corporations engaged in any hazardous form of business, such as mining or producing oil.

Owing to the uncertain nature of such business, the annual profits fluctuate greatly, except in the case of very large corporations whose business is on such a scale that the element of chance is practically eliminated and whose annual earnings, therefore, are fairly uniform and approximate the average profit of the business. The smaller companies do not do the volume of business to obtain such a uniform rate of profit each year. Their profits depend largely on chance or luck, and it is often the case that they have several bad years of little or no profit, and then, due to a lucky strike, an exceptionally good year showing a very large profit for that year, which profit may be very badly needed to average up with the lean years.

To illustrate how the proposed new rates might work. A large company makes 20 per cent profit each year for five years; a small or medium-sized company averages 20 per cent profit for five years the same as the large company, but it makes only 5 per cent profit during four of these years and then 80 per cent in the fifth year.

Large company.

Profits.	Tax.	Percentage of tax on invested capital.
<i>Per cent.</i>	<i>Per cent.</i>	<i>Per cent.</i>
8	.....	2.45
7	20	2.50
5	35½	
20	.....	4.95

Medium company.—Four years, 5 per cent annual profit; no tax; one year, 80 per cent profit.

Profits.	Tax.	Percentage of tax on invested capital.
<i>Per cent.</i>	<i>Per cent.</i>	<i>Per cent.</i>
8	.....	.....
7	35	2.45
5	50	2.50
60	70	42.00
80	.....	46.95

Average for 5 years, 9.39 per cent.

It will be noted that the smaller company, with the same average percentage of profits, pays nearly twice as much excess-profits tax as does the large company. Or, to put it in another way, the large company pays in excess-profits taxes about 25 per cent of its profits and the smaller company nearly 50 per cent.

The difference would be still more marked if in some years the smaller company should not have profits, but losses. If it sustained a very serious loss involving a large portion of its capital, it could, with these excess-profits taxes (which, too, would be greatly augmented on account of the company's dwindled invested capital) never possibly recover, no matter how fortunate it might again be in another year.

Being engaged in the oil-producing business, and realizing the great ups and downs of the same and the tremendous risks that have to be taken in this business and the great losses that are part of this business, I seriously fear the excess-profits tax will hurt so severely the smaller companies engaged in this business that many can not survive.

The large companies will get along all right because, on account of their large volume of business, they will earn fairly uniform profits, and therefore are less likely to have to pay any taxes at the higher rates; also, because, as a rule, they are heavily capitalized.

Herein seems to lie the serious defect of the excess-profits tax. It bears most heavily on small and conservatively capitalized concerns, and the larger a company is and the more it has been capitalized, and possibly overcapitalized, the less is the burden.

How can smaller concerns, engaged in hazardous business and so handicapped, compete with the great corporations?

It is my understanding, although I am not sure it is true, that the English law allows a refund to taxpayers who, having paid heavy excess-profits taxes, in subsequent years sustain losses or greatly reduced earnings. This idea would seem to have a merit, and, if it could be carried out, would doubtless in the future save many concerns and enable them to continue in business.

Yours, very truly,

G. A. FORMAN.

(The chairman here presented a letter in the nature of a brief from the National Association of Cotton Manufacturers, which is printed in full, as follows:)

THE NATIONAL ASSOCIATION OF COTTON MANUFACTURERS,
Boston, Mass., September 18, 1918.

Hon. F. M. SIMMONS,
Chairman Finance Committee, United States Senate,
Washington, D. C.

SIR: The National Association of Cotton Manufacturers, through its taxation committee, begs to submit to you the following as its views upon the new war revenue bill drafted by the Ways and Means Committee of the House and now under consideration by your committee:

It is the belief of the National Association of Cotton Manufacturers that extremely important economic fundamentals have been almost entirely neglected by those who, up to the present time, have had the measure in hand. Speaking

in the broadest way, the entire bill rests upon the assumption that when a nation is engaged in a war, the larger the part of the cost of the war that is met out of the current income of the nation during the war period itself, the sounder the economic condition of the nation is kept, both during the war and in the years succeeding the war.

As a basis for this assumption, much has been made—and a few professional economists have lent their weight to the contention—of the argument that, inasmuch as the materials of all kinds required for the prosecution of the war must clearly come out of the nation's current production of goods, therefore, these materials should be paid for out of the current income of the nation. It is declared that the customary process by which important enterprises are carried through in peace times, i. e., the use of materials currently produced but paid for in subsequent years through the machinery of credit—is contrary to the public welfare in war time. Accordingly, it is asserted, despite the fact that the war itself, through its withdrawal of millions of men from their usual activities in the way of multifarious production and service, actually (if not in terms of money, since price inflation is a usual accompaniment of war), very greatly reduces the national income, the war period ought to be marked by an enormously greater reduction in the part of this national income which is regularly applied to the normal production and consumptive uses of the community than was the case in the prewar peace days or than is contemplated for the postwar period. Whereas the entire economic fabric of the modern world has been built up through resort to the use of credit to the greatest possible extent for the distribution of economic strains and stresses over long periods of time, in order that these stresses and strains may not be thrown all in a moment upon the community, absorbing so much of its current income as to impair its productive efficiency, the new doctrine of war finance seems to hold that the very reverse of this practice should be employed in war time, the abnormal economic strains and stresses of the war being met at the moment of their occurrence by the severest reduction in the part of the national income left free for normal uses which the population will endure.

It must, of course, have been largely by rule of thumb that the proportionate distribution between taxation and credit of the current year's war costs of the United States was arrived at by the administration and the Ways and Means Committee. There is no discoverable basis in the available statistics of the country's wealth and national income as a whole, or of the wealth and income of the various classes of persons and productive instrumentalities (corporations, etc.) in the country, for the determination of the apportionment of the total estimated war costs of \$24,000,000,000 (including loans to our allies) in the proportion of one-third (\$8,000,000,000) ~~and~~ from the Nation's income (taxation) and two-thirds (\$16,000,000,000) from the country's savings and credit resources (liberty bonds, war savings, and thrift stamps, etc.). Economically speaking, the most that can be said of the proportions, one-third taxation (for the country's war expenses on its own account the proportion is near one-half) and two-thirds borrowing, is that, besides being convenient round amounts, they outdo, in respect of the relative largeness of the taxation and the relative smallness of the resort to credit, the figures of any other nation in this or any other war. In other words, the proportions carry out, to the largest extent thought endurable for the country's population, the new and so-called "ideal" theory of war finance.

It may be remarked in passing that there is a certain economic incongruity between the \$8,000,000,000 a year set by the Ways and Means Committee as the proper measure of taxation while the war is actually being fought and its disturbance of the national economy is at its height, and the \$4,000,000,000 of annual taxation which the committee's chairman, Mr. Kitchin, has recently stated to be the probable annual rate when the war is over and our armies have returned to their usual productive occupations and services at home. The question inevitably arises why, with the greatly reduced number of producers of the war period, the population should be called upon to pay when the number of producers has been restored by the termination of the war? The answer that, while we are actually at war we are compelled to meet inordinately heavy immediate expenses, while after the war is over we shall have to meet, more or less at our leisure, only the interest and amortization costs of that part of our war expenditure which we have obtained by borrowing (plus, of course, pensions or their equivalent, and some other charges having a war origin), is very far from convincing. It is of supreme importance to the national economy,

in fact, that such extraordinary wide alternations of relatively heavy and relatively light annual drafts upon the current national income should be avoided, or at least mitigated, to the utmost possible extent, since the disarrangements and impairments which they occasion—and particularly which the heavy drafts, suddenly thrown on, occasion—far outweigh in importance any and all gains derived from making the population, as a productive entity, for a time “pay as it goes” an inordinately large part of current expenses which it is compelled to meet. In it lies the primary function of credit in the interest of the general productive efficiency, and hence in that of the public welfare, to lessen the harmful pressure of sudden increases of exigent expenses by distributing such increases over longer periods of time and enabling them to be met by the community out of its future as well as its present production. It is in accordance with this principle that all the great enterprises of this and other countries have been carried through in modern times, and it is in reality idle at this late date to assert that the entire system is wrong and should be replaced by one permitting the least possible use of the machinery of credit and the maximum possible expenditure or tying up of current income.

It is for these reasons that the entire theory upon which rests the distribution of the country's war expenses on the basis of one-third (actually nearly one-half) taxation and two-thirds borrowing, is open at least to the gravest doubt with respect to its harmony with the best teaching of modern experience in the matter of the financial and fiscal methods most conducive to the maintenance of the productive economy of nations unimpaired through the severest stresses and strains. Nations, like important public and private enterprises of less scope, do best for themselves when they use credit, in so far as this is possible, as a mean of distributing abnormally heavy present costs over relatively long future periods of national production. And if, in a spirit of supposed self-sacrifice or of idealizing effort to keep as close as they can to that traditionally excellent condition of “being out of debt,” they undertake the reverse practice, they will find that the outcome in the end is the same for them as it would be for a private enterprise following the same rule.

Much has been said in this country of the excellence of the methods pursued by Great Britain in her war finance, especially as regards the comparatively high proportion of the cost of the war for her, which she has met from the proceeds of taxation. One of the specific objects of our own lawmakers seems to be to outdistance Great Britain in this respect. Yet the student of the fundamentals of national economics will doubt whether the praise lavished upon Great Britain's war finance is really merited.

It is commonly assumed on this side of the Atlantic that British war finance is far sounder than French war finance for the very reason that the French have kept their taxation down to the irreducible minimum necessary to meet the permanent charges in the way of interest on debt, pensions, etc., which the war has imposed and is still imposing on the country. The French, however, are the most lucid of all nations in the matter of financial and fiscal thinking, as in so many other directions; and as the expert studies the position in which France will probably be left at the end of the war, comparing it with the probable position of Great Britain, he finds it hard to avoid the conclusion that in the end the national economy of France as a whole will be found to have been relatively less impaired by the war than that of Great Britain—and this in spite of the vast destruction of industrial equipment and the extensive interruption of industry which France has had to endure. Economically, France is in a less constricted condition to-day—has a greater freedom of movement financially and industrially—than appears to be the case with Great Britain. So far as we can foresee what will occur in the various belligerent nations at the end of the war, France will make her new start decidedly more easily than will Great Britain, though she is naturally much the poorer nation, and besides has suffered far greater mutilation at the hands of the common enemy. And for this advantageous position of France the avoidance of excessive taxation during the war, even at the cost of a proportionately heavier debt at the conclusion of the war, will be to a large extent responsible.

Though it can not truly be said either of the heavy taxation proposed by the Ways and Means Committee or of that imposed by the British Government that the national incomes of the respective nations can not endure such levies without acute distress for the population as a whole and serious risk of a general economic breakdown, the practical conditions under which the levies have to be imposed in war time are of a character to yield a maximum of economic harm. Thus it is practically impossible to devise adequate machinery, amidst the

pressing necessities of the war itself, whereby every class in society, from the lowest to the highest, can be made to contribute its proportionate share of the great sum total. War will not wait for the constructing and perfecting of this machinery: its demands are peremptory and immediate. Hence the lawmakers inevitably turn at once for much the greater part of the expected tax yield to the particular limited classes of persons and economic instrumentalities from which the largest amount of liquid return can most easily be derived. Taxes on individual incomes and profits of corporate enterprises answer this description, and it is upon them that the great burden of taxation is inevitably imposed.

When this is done, however, a collateral result of the gravest consequence is immediately obtained—a result that almost at a stroke deeply impairs the general national economy. In so far as the proceeds of taxation of this kind involve a reduction of the net yield of income-producing properties, the market value of these properties immediately reflects, by the process known as "capitalization," the loss of net yield; and while the properties may remain physically and productively as good as ever they were, their value to their owners, especially as a basis for credit, is very much less. Thus the raising of the British income-tax rate at the beginning of the war was soon followed by a decline in the aggregate value of 387 selected and seasoned securities on the London Stock Exchange, of over 20 per cent, or nearly \$3,500,000,000. Similarly our own income-tax laws have reduced the market value of securities dealt in on the New York Stock Exchange in an amount of approximately \$5,000,000,000, while the market worth of urban real estate in this country has notoriously declined on the average by some 15 or 20 per cent, and in some large cities by nearly 30 per cent. Thus, while there has been a very great enhancement in the market values of primary commodities and articles of manufacture and trade in both the United States and Great Britain as a result of war conditions, the particular forms of war taxation necessarily adopted by the two countries to give the high tax yields desired have probably to quite as great an extent reduced the market values of the countries' income-producing properties, and in this wise impeded tremendously the provision of the credit resources upon which, after all, the respective Governments must for the most part rely. Hence come all kinds of uncomfortable conditions in the securities markets in general, and especially in the markets for the great war loans that have been or must be floated. This point is perhaps best illustrated by the disparities in the quotations of the liberty loan bonds of the United States—disparities which are only too likely to become greater and more harassing to the Government as the process of adjustment of the market prices to the net yields for so-called "marginal" purchasers approaches completion.

These "marginal" purchasers in the securities markets are, of course, those wealthy persons known as speculative, rather than permanent investors, who make it their business, in whole or in part, to buy and carry the floating supply of the various securities, Liberty Loan bonds among the rest. The great majority of these "marginal" purchasers are called upon to pay high rates of income tax and surtaxes; and with every increase of these rates they reduce the prices at which they are willing to carry the floating supply of securities, in order that the net yield to them may be the "going" rate for investment capital. It is by this process, or one essentially the same, that the market values of all forms of income-producing property are slowly but surely reduced by heavy and increasing income taxation. And the further this process goes, the more the permanent credit resources of the country are reduced, because these properties in the last resort serve as the basis of the permanent credit resources, just as commodities in process of distribution serve as the basis of short-time or commercial credit resources.

What has just been said brings out the general principle that is made operative by the chief forms of taxation embodied in the war revenue measure now before your committee. Something should be said, however, of the illusory notion that these forms of taxation are peculiarly effective in restricting so-called "inflation," whether price inflation or, as a sequel to price inflation, monetary inflation. Nothing could be further from the truth than this notion. There is not the faintest evidence that price inflation has its beginning in the increased buying of the well-to-do classes, whose number and aggregate consumption are too small to have an appreciable effect upon the movement of prices, except those for a few pure luxuries. Domestic price inflation invariably has its origin in an increased purchasing power and in actual increased purchasing of the great mass of the community, who can be reached by taxation in the actual period of a war by no government, because no gov-

ernment has or can devise quickly enough the elaborate machinery necessary. One qualification should perhaps be made at this point, i. e., that by general consumption taxes the mass of the population can be reached and made to reduce its purchases.

Turning now from the larger aspects of the new war-revenue bill to the taxes imposed by the bill upon corporations, it may be said at the outset that the entire treatment of what is designated as "invested capital" in the bill is without economic justification. The true invested capital of a business enterprise consists of the sum of the following items: (1) Value of lands, buildings, and machinery; also patents and good will; (2) value of raw materials on hand; (3) value of goods in process; (4) value of outstanding accounts and bills receivable; (5) cash. It makes not the slightest difference whence came the funds, when they came, or in what form they came, from which the above values are derivable. In any case, the sum of these values is the actual "invested capital" of the business. The complex elaborations, differentiations, and so on of the bill, in its attempt to give a catch-all definition of "invested capital," do no more than give rise to inequalities, injustices, and absurdities. We trust your committee will effect abandonment by Congress of this incoherent and, in many respects, wholly senseless treatment of the subject of "invested capital."

A further economic absurdity of the bill is its treatment of "excess" profits. The phrase "war profits" means something intelligible and at the same time real; for it is certainly possible to see in the enhanced profits of many enterprises an element—often a very large one—which is undeniably attributable to the war and to nothing else. The moral feeling of the community is undoubtedly—and in most cases properly—averse to the making of profits purely and simply out of war, which means loss and suffering for the vast majority; and the heavy taxation of profits arising from this source alone has the sanction not only of society at large, but usually of the very persons or enterprises called upon to meet such taxation.

The phrase "excess profits," on the other hand, is an entirely meaningless one, except where actual monopolies are involved. Wide differences in earning power, as between different individuals and different business enterprises, are indubitable facts of nature, and must be recognized as such by any sound polity. The high earnings of the skillful, the enterprising, the inventive, the farseeing, are not "excess" profits; for without them we should soon have all economic activity at a standstill and the case of society would be desperate indeed. Accordingly, there is no economic defense—and in reality no social defense—for the general treatment of profits above the average, or "excess" profits, in the new war-revenue bill.

We feel that American business men should stand out against this part of the bill as a matter of the highest ultimate welfare of the country.

Very truly, yours,

RUFUS R. WILSON, *Secretary.*

DRUGS.

The CHAIRMAN. The committee will now hear Mr. Eugene Brokmeyer.

STATEMENT OF MR. EUGENE C. BROKMEYER, COUNSEL FOR THE NATIONAL ASSOCIATION OF RETAIL DRUGGISTS.

Mr. BROKMEYER. Mr. Chairman and Senators, my name is Eugene C. Brokmeyer, and I am general attorney for the National Association of Retail Druggists, and speak for the 50,000 druggists of the country.

Senator Smoot has said he supposed I would like to address some of my remarks to the proposed repeal of section 6 of the Harrison Act. It seems rather a curious and odd occasion to discuss narcotics when your committee is considering revenue measures, and it was rather a surprise to the drug trade that the pending revenue bill should have been made the occasion for an attempt to repeal section 6 of the Harrison Act, after you gentlemen and Congress spent so

much time with the Harrison Act three years ago, and thrashed it out thoroughly.

Senator THOMAS. You know the basis of the action of the Ways and Means Committee is that the act, as we then passed it, has not proven effective in practice.

Mr. BROKMEYER. Senator, I am quite familiar with that contention, and the answer is simply this, that the evidence submitted to the Ways and Means Committee was submitted by some representatives of the Internal Revenue Department, and the decision of the Ways and Means Committee is based entirely on ex-parte testimony. The drug trade have not had an opportunity to analyze that testimony, or to rebut it.

Senator SMOOT. The mere repeal of it will do a great deal more harm than it will do good.

Mr. BROKMEYER. Exactly.

Senator LODGE. Will you point out the clause in this bill which repeals the Harrison Act?

Mr. BROKMEYER. Yes, sir. Page 154, at the bottom of the page, section 1009 [reading]:

That section six of such act of December seventeen, nineteen hundred fourteen, is hereby amended to read as follows:

"Sec. 6. That the provisions of this act shall not apply to decocanized coca leaves from which all cocaine and other related alkaloids or associated salts have been extracted, nor to preparations of such decocanized leaves."

Senator SMOOT. That is the milk in the coconut.

Mr. BROKMEYER. That simply means that all the other provisions of section 6 are repealed.

The other provisions repealed represent the exemptions of all the narcotics laws of every State and Territory in the Union. The exemptions were suggested and recognized by the International Opium Convention, article 9 of which said that it was the purpose of the treaty powers, including this country, to regulate and control the use of habit-forming narcotic drugs, but not to so restrict them as to interfere with legitimate and medical uses, and Congress, recognizing that, in the passage of the Harrison bill, very wisely incorporated the exemptions of section 6. For years information, these exemptions, in a few words, simply provide that preparations containing negligible quantities of narcotics, when mixed with ingredients of medicinal virtue, possessed and used, administered in good faith, and not for the purpose of evading the provisions of the Harrison law, shall be exempt from the provisions of the Harrison law. That is section 6. And under those exemptions it has been thought that preparations containing these negligible quantities, which experience shows renders them impossible to become habit-forming, and which the House committee's report at the time, in explaining section 6, said it was the purpose of Congress to exempt for the reason that the quantities which they contain were negligible, and when mixed with medicines in these small quantities could not become habit-forming, should not be subjected to the provisions of the act, the purpose of the act being to control the use of narcotics.

Senator THOMAS. What have you to say as to this statement of Mr. Kitchin in the report to the House [reading]:

Under the present law only prepared smoking opium seized by the United States Government from any person violating the acts of October 1, 1890, as amended by the acts of March 3, 1898, February 9, 1909, and January 7, 1914,

may be sold to the highest bidder, pursuant to the provisions of section 3460 of the Revised Statutes of the United States. The Secretary of the Treasury does not have any authority to dispose of coca leaves, their salts, and derivatives, or compounds, or opium, except smoking opium, in any manner whatever, when seized for violation of any of the above acts, or when seized under the act of December 17, 1914. Neither are the courts authorized by any statute to dispose of coca leaves, their salts and derivatives or compounds, or any opium, except smoking opium.

Mr. BROKMEYER. I think that is a wise provision. We have no earthly objection. Our protest is simply against the repeal of section 6.

Senator LODGE. I do not understand how that repeals section 6.

Mr. BROKMEYER. By simply amending section 6 so as to preserve the particular clause here that is written in the bill. All of the other provisions of section 6 are excluded by this amendment.

Senator SMOOT. All the proprietary medicines were excluded, as the gentleman has said.

Senator LODGE. This applies only to coca.

Mr. BROKMEYER. It now eliminates that exemption that we intended to make for these proprietary medicines.

Senator TOWNSEND. Who has section 6 here?

Mr. BROKMEYER. I have it in a brief which I was going to file.

Senator PENROSE. Let section 6 be read in the record.

Mr. BROKMEYER. Here is section 6, for your information, if I may be permitted [reading]:

Section 6. That the provisions of this act shall not be construed to apply to the sale, distribution, giving away, dispensing, or possession of preparations and remedies which do not contain more than two grains of opium, or more than one-fourth of a grain of morphine, or more than one-eighth of a grain of heroin, or more than one grain of codeine, or any salt or derivative of any of them in one fluid ounce, or, if a solid or semisolid preparation, in one avoirdupois ounce; or to liniments, ointments, or other preparations which are prepared for external use only, except liniments, ointments, and other preparations which contain cocaine or any of its salts or alpha or beta eucaine or any of their salts or any synthetic substitute for them: *Provided*, That such remedies and preparations are sold, distributed, given away, dispensed, or possessed as medicines and not for the purpose of evading the intentions and provisions of this act.

Our contention is that if any of these preparations containing these negligible quantities should perchance be used in gross quantities to satisfy the craving of an addict, and the Treasury Department has any evidence of that fact, that evidence is proper evidence for the Department of Justice, upon which a conviction may be obtained. But we do not admit that these preparations can be consumed in sufficiently large quantities, for the reason that they are mixed with ingredients of medicinal properties, and if taken in large quantities they would be ejected from the system either by nausea or otherwise.

Senator THOMAS. The report in regard to that particular section recites that [reading]—

In the administration of the act it has been found that the exemption has made the adequate enforcement of the act almost impossible, and that many preparations are marketed which contain a lawful amount of the drugs, but which are of great harm to the consumer.

Mr. BROKMEYER. In reply to that our answer to the Internal-Revenue Department, when it made that contention, was that we asked them whether they had submitted evidence upon which that state-

ment as made, and upon which the Ways and Means Committee predicates that statement to the prosecuting officials in an attempt to secure conviction, and it was found, as far as I have been able to learn—I confess I was not given definite information—that the evidence was collected and held by the Treasury Department's representatives for the very purpose of preparing this case which they have submitted, and that a bona fide attempt has never been made to secure convictions.

Senator LODGE. What was the proportion of opium in that section?

Mr. BROKMEYER. It varies with the different narcotics. In the case of opium it is two grains.

Senator LODGE. One-quarter of a grain of morphine is pretty big.

Mr. BROKMEYER. To two ounces. Let me call your attention to this fact, that a reputable physician of Washington, re-writing a popular remedy for cold for a patient of his, who was a client of mine, prescribed one-quarter of a grain of morphine to 1 ounce of mixture, using other ingredients suitable for a cold, and that did not produce an addict, and any reputable physician does that right along.

Senator SMOOT. Senator Thomas was chairman of the subcommittee that had that Harrison bill up for consideration, and we gave days of hearings upon the question as to the quantities in that bill, and it was decided by every person who was before the subcommittee that those quantities named in the Harrison bill were not detrimental, and would no form and could not form a drug habit.

Mr. BROKMEYER. And the best proof is that all the States of the Union have identically the same thing in their narcotic laws, and it is a reasonable presumption that their experience perhaps has dictated that.

Senator LODGE. Your objection to this thing is its wording, that it sweeps away all of that.

Mr. BROKMEYER. It wipes it out entirely.

The CHAIRMAN. Was not that unintentional?

Mr. BROKMEYER. No, sir; it was apparently deliberate; and perhaps it might be well, for your information, to say that this was brought about by the Deputy Internal Revenue Commissioner, Mr. Keefe, and his assistant Dr. Reese, who was charged in the administration of the Harrison law regulations, with preparing this bill, submitting it to Mr. Rainey, who adopted it for them and introduced it in the House; and then before the bill was reported to the House, when we got copies of the bill and asked for a hearing, Mr. Moore of Pennsylvania told us that it was unfortunate, that we were too late; that the bill had been incorporated in the revenue bill without a hearing; whereas, three years ago, due to the kindness and indulgence of your committee here and of Mr. Burton Harrison of the Ways and Means Committee we were given practically a year with Dr. Harrison Hamilton Wright fully considering all this, and Dr. Wright explained it to the retail druggists, and later went on record as joining one of the speakers in his opinion this morning, and Mr. Black has asked that the tax on medicines be made 4 per cent rather than 2, for the reason that although the consumer pays the tax the druggist is vitally interested, and that no tax shall be imposed that will have the effect of decreasing the volume of his business. We feel that if an exorbitant or unduly high rate is imposed in addition to all the other costs, the high cost and advanced costs of drugs, and many

other items, the business of the druggist will become so small that it will be difficult for him to continue.

Place this 10 per cent tax proposed in the bill on proprietary preparations. Of course you understand every preparation made by a druggist according to his own formula, not only patent medicines, but everything made by a druggist in his own shop and according to his own formula, is under this tax, because the provision in the law is so broad as to include that. This tax, I say, in addition to doubling the alcohol tax—you understand the druggist uses alcohol in compounding prescriptions; it is one of the most widely used articles that he handles, and while the tax on proprietary medicines is paid by the consumer and the proposed tax on nonbeverage alcohol used by the druggist in compounding his prescriptions will be put on the prescriptions, we fear that the cost to the druggist himself will so decrease the volume of his business that the druggist can not continue.

Senator TOWNSEND. How do you think that would effect the people as a whole, to decrease the amount of drugs that they use?

Mr. BROKMEYER. The effect on the prescriptions alone would be to double the cost of prescriptions, which already has been doubled as the result of the high price of alcohol.

Senator TOWNSEND. I am thinking of the health of the people as a whole, if they did not use but half the amount of drugs they now use, would it not be better for them?

Mr. BROKMEYER. That is something that each person must answer for himself. I assume that the development of the pharmacy and of the practice of the physician and all those things express what people require, or at least what they demand, so that that is problematical.

Senator ROBINSON. Have you investigated the question as to the profits that are usually made on retail drug transactions?

Mr. BROKMEYER. In a casual way only; but I can say this, that if it seems that profits are high, I have here a few items showing the advance in cost of the drugs to the druggists since the beginning of the war.

Now, ammonia, which before the war could be bought by the druggist for 81 cents a pint, he now pays \$1.50 a pint for—ammonia being very generally used.

Digitalis, which before the war cost 81 cents a pint, now costs \$1.60.

Belladonna has been increased from \$1.25 to \$1.88.

Spirits of camphor has increased from \$1.20 to \$2.20.

Essence of pepsin has increased from \$1.60 to \$2.60.

Senator ROBINSON. I understand about that.

Mr. BROKMEYER. Yes, sir.

Senator ROBINSON. But the inquiry I am making is, the point that is implied in my question is, that the retail drug trade as a whole is enormously profitable, considering the amount that is invested in it. I have made some investigation into that, and my inquiry leads me to believe that very great profits indeed are made on drugs.

Mr. BROKMEYER. I might call your attention in relation to that, as a member of this committee, to the fact that druggists are compelled to sell sandwiches and tea, and chocolate and coffee in their places of business, so that the modern drug store can hardly be recognized as an apothecary's shop, and I take it they are compelled to do that in

spite of themselves, because I assume that seeing they are specially qualified and trained men in their profession, it must be humiliating to them to do it, and they would not do it if they did not have to.

Senator ROBINSON. I do not think that is true. I think the ordinary drug store in the country town sells its products at 150 to 250 per cent profit. I do not think you ought to complain about a small tax like this, if that is the case.

Senator TOWNSEND. I will give you an instance. I have an instance that has given me some little disturbance, and perhaps you can give me some information on it. I was advised by a reputable doctor to get a bottle of Squibb's Pectrolatum. I had bought some of that before the war. As I remember, I paid 40 or 50 cents a bottle for it.

Senator SMOOT. What sized bottle?

Senator TOWNSEND. It is a pint bottle, I think. It is the same bottle that I had seen. There are two drug stores in the block where the Portland Apartment House is. One drug store is out on Thomas Circle and the other is at the other end of the apartment house. I stepped into one of those drug stores and asked the price of a bottle of this medicine and was told it was \$1.25. I thought it was a pretty large amount, so I went down to the other drug store, and they told me there that it was 85 cents; the same brand of product; one store charging \$1.25 and the other 85 cents. I wonder what law of reason or of the war it was that made those prices differ.

Mr. BROKMEYER. I know nothing about the conditions in this particular case, but I want to assure you that the experience of druggists differs, particularly as to the effect of the draft. Some have qualified help and others have not. Some, who are able to get qualified help are paying to-day two or three or four times for it what they paid before.

Senator McCUMBER. There is no standard, is there, by which druggists agree upon what a prescription costs, but each one charges what he thinks he ought to get?

Mr. BROKMEYER. He can not, under the law, agree with his competitors.

Senator McCUMBER. There is no price fixing?

Mr. BROKMEYER. He can not agree, under the Sherman law. Now, just before leaving that proprietary-medicine tax, the druggists are interested in the alternative proposed, which allows the Commissioner of Internal Revenue to collect the tax in the form of a stamp, paid by the purchaser and affixed by the vendor. I have no fault to find, though the druggists would naturally contribute their time and trouble to that part of it; but the other provision, which requires the druggist to collect the tax, to keep records and make an inventory and make returns, will impose upon him additional burdens.

Senator THOMAS. Two years ago the people whom you represent complained very strongly because they were required to place these stamps upon their commodities.

Mr. BROKMEYER. You are quite right, Senator; that is a fact.

Senator THOMAS. They said that it required so much time that it would be unjust.

Mr. BROKMEYER. That is true, and we would be opposed to a stamp tax to-day if it were not that we realize we have got to make our sacrifices and contribute our part toward the general war program.

There is just one other part of the bill I want to speak of, and that relates to the tax on soda fountains. The bill fixes a tax on 7-cent drinks, 1 cent; from 7 cents to 10 cents, 2 cents; and with the tax on the drinks selling at 7 cents we have no fault to find.

Senator THOMAS. There is a temptation to charge 15 cents instead of 10 cents; that is the objection I see there.

Mr. BROKMAYER. There is a limit as to what we can charge.

Senator THOMAS. What is the limit?

Mr. BROKMAYER. It depends on the druggist's customers what he dares charge.

Senator THOMAS. That is it exactly. This 1 cent stamp tax will probably result in the imposition of an increase of 100 or 200 per cent on the consumer.

Mr. BROKMAYER. Here is what I was getting at. If you will impose a tax of 1 cent for every 10-cent drink, and you will make it 2 cents for every drink selling between 10 cents and 20 cents, you will get more revenue for the Government, because you will take care of the most popular of all drinks—that is, the ice-cream soda.

Senator THOMAS. My objection to that is that I think it can be used to increase very greatly the cost to the consumer and to increase the profit to the vender, beyond what he would otherwise realize.

Mr. BROKMAYER. That is true; but if he increases his prices too much he will destroy his trade. Ice-cream sodas are up to 15 cents, and the effect of this would be to put a 4-cent tax on a 15-cent ice-cream soda, which would make it 19 cents; and the druggists honestly tell me that if they were to charge 19 cents all over the country they would not sell ice-cream soda. The effect of that would be to drive people to the 5-cent drinks. That would mean that the Government would get more revenue from the 1-cent tax.

Senator THOMAS. Will there be such a thing as a 5-cent drink after this of any kind.

Mr. BROKMAYER. Yes. Five-cent drinks may go to 7 cents, but they will not go over that.

Senator THOMAS. Do you know of any such thing as a 5-cent drink?

Mr. BROKMAYER. Oh, yes; Coca Cola and things like that. But my idea is that if you will apply the 2-cent tax to the drinks selling between 10 cents and 20 cents you will preserve the trade as it is to-day, and you will get for the Government the income from the 2-cent tax; whereas if you keep the provisions as they are here you will drive people to the lower priced drinks.

Senator THOMAS. That would allow you to have a 10-cent drink and pay the tax?

Mr. BROKMAYER. Yes. I will ask permission to submit a brief.

(The brief referred to by Mr. Brokmeyer is here printed in full, as follows:

NATIONAL ASSOCIATION OF RETAIL DRUGGISTS,
Washington, D. C., September 12, 1918.

THE FINANCE COMMITTEE, UNITED STATES SENATE,
Washington, D. C.

GENTLEMEN: The National Association of Retail Druggists, speaking for all of the drug stores of the country, upon which the public depends for the compounding and dispensing of necessary drugs and medicines, and many other things, respectfully protests against the proposed amendment of the Harrison Narcotic Act (an act of Congress approved Dec. 17, 1914) in the form of a

"rider" tacked onto the pending revenue bill without notice to the drug trade and pharmacy interests and an opportunity to be heard before the Ways and Means Committee of the House had determined the matter on testimony submitted alone by representatives of the Internal Revenue Department.

The proposed amendment was prepared by the Treasury Department, introduced in the House of Representatives as H. R. 12787 a few days before the revenue bill was reported by the Ways and Means Committee and incorporated bodily in the revenue bill without discussion by practical drug and pharmaceutical men, who alone might have intelligently advised all of the members of the Ways and Means Committee as to the effect of the proposed amendment on drug and pharmaceutical interests and the public welfare. Your honorable committee will recall how you considerably and wisely cooperated with representatives of all branches of the drug trade and pharmacy before the Harrison Act was enacted, in order that no injustice be done the public and drug and pharmaceutical interests in the manufacture and sale of habit-forming narcotic drugs when used for legitimate and necessary purposes. It is noteworthy that the Ways and Means Committee of the House also cordially cooperated with the representatives of drug and pharmaceutical interests before the enactment of the Harrison Act, with gratifying results to all concerned.

Sections 1008, 1009 and 1010 of H. R. 12863, Union Calendar No. 256, are the sections which incorporate the Rainey bill, to be found on pages 149, 150, 151, 152, 154, 155 and 156. Under the guise of a revenue measure these sections are no more or less than a proposed exercise by the Federal Government of the police powers of the several States, guaranteed to them and to them alone under the Federal Constitution. While most of the Rainey bill is devoted to prescribing the rates of taxation and the method of collecting the taxes proposed, next to the last section, section 1009, repeals section 6 of the Harrison Act except a provision exempting decocainized coca leaves and preparations containing them from the provisions of the act. That part of the Harrison Act repealed is as follows:

"SECTION 6. That the provisions of this act shall not be construed to apply to the sale, distribution, giving away, dispensing, or possession of preparations and remedies which do not contain more than two grains of opium, or more than one-fourth of a grain of morphine, or more than one-eighth of a grain of heroin, or more than one grain of codeine, or any salt or derivative of any of them in one fluid ounce, or, if a solid or semisolid preparation, in one avoirdupois ounce; or to liniments, ointments, or other preparations which are prepared for external use only, except liniments, ointments, and other preparations which contain cocaine or any of its salts or alpha or beta eucaine or any of their salts or any synthetic substitute for them: *Provided*, That such remedies and preparations are sold, distributed, given away, dispensed, or possessed as medicines and not for the purpose of evading the intentions and provisions of this act."

The foregoing section is substantially the exemption provision of all the narcotic laws of the States and Territories of the Union, which are based upon the practical experience of the people of this country and have stood the test of many years' operation.

The language underscored in section 6 was used by Congress to make it impossible for any person to abuse the exemption provisions and privileges of section 6 without subjecting himself to the penalties of the law, and if the Treasury Department has evidence of abuses of the law, it should be called upon to explain why this evidence has not been furnished the Department of Justice for purposes of prosecution.

The repeal of section 6, as proposed, would nullify one of the purposes of the International Opium Convention, which is "to limit the manufacture, the sale, and the use of morphine, cocaine, and their respective salts to medical and legitimate uses only," as declared in article 9 of the treaty. The proposed repeal of section 6 would seriously interfere with rather than limit the manufacture, the sale, and the use of narcotic drugs for medical and legitimate purposes, and it was because your honorable committee and the Ways and Means Committee appreciated this fact that Congress wisely incorporated section 6 in the Harrison bill when it was enacted.

The proposed repeal of section 6 would also conflict with the purpose of Congress as declared in House Report No. 23, Sixty-third Congress, first session, as follows:

"There is a real, and one might say, even desperate need of Federal legislation to control our foreign and interstate traffic in habit-forming drugs, and

to aid both directly and indirectly the States more effectually to enforce their police laws designed to restrict narcotics to legitimate medical channels."

The same purpose as stated in the foregoing House report is recorded in Senate Report No. 258, Sixty-third Congress, second session.

In other words, the intent of Congress in the enactment of the Harrison act was to aid the States, not usurp the police powers of the States, in the enforcement of laws limiting narcotics to legitimate medical uses, and for other recognized necessary purposes.

It is contended that conditions have changed and that thousands of addicts have been found of draft age in Baltimore and New York City. Granting this to be true, it certainly does not follow that the large number of these addicts should or can be attributed to the abnormal use of preparations containing narcotics in negligible quantities as provided in section 6. In fixing responsibility it would be more reasonable and fair to take the Treasury Department at its own word when it reports in successive annual reports of the Internal Revenue commissioner that far more violations of the Harrison act have been committed by physicians than by druggists or any other class. It is more probable that these addicts, like all other addicts, were created by the administration of narcotics upon the prescriptions of physicians than otherwise, because it can easily be established that the consumption of preparations containing a narcotic in a quantity exempted by section 6 in any considerable quantity would result in nausea, or some other form of elimination of the preparation from the human system. Recognizing this obvious fact, Congress explained the exemptions of section 6 in the House report referred to as follows:

"Section 6 exempts from the provisions of this act preparations and remedies which contain so small a proportion of narcotics as to render it impossible that they should become habit-forming drugs."

The Senate also concurred in this report, when submitted by your honorable committee.

The contention of the Treasury Department that 35,000 gallons of paregoric were sold in 15 States within three months should not be regarded as serious, or significant. The department does not state the purposes for which the paregoric was sold and therefore there is no way of determining whether it was used for legitimate and necessary purposes, or not. It certainly does not follow that all of it or any considerable part of it was used for illegitimate purposes, in the absence of proof to that effect. There are anywhere from fifteen to twenty million persons in 15 States and this large population surely needs a considerable quantity of this popular and widely used preparation. Thirty-five thousand gallons equals 4 480,000 ounces, or 2½ drams per person in three months, on the basis of a population of 15,000,000 persons, the lowest estimated population of 15 States. One ounce of paregoric contains 1.8 grains of opium, so that assuming that one person consumed 2½ drams of paregoric in three months and that every one of the 15,000,000 persons consumed paregoric, each person would have consumed less than one-half a grain altogether in that length of time. Nor would he have consumed one-half a grain of opium in its state as opium. Paregoric contains benzoic acid, camphor, and oil of anise in quantities proportionately the same as that of the opium content, to which is added a small percentage of glycerine, the remainder of the preparation consisting of diluted alcohol. To consume paregoric, therefore, in any considerable quantity, or in sufficient quantity to satisfy the craving of an addict, would undoubtedly result in the consumer's illness, or in the rejection of the preparation by the system before its effect could be felt. Repeated experiences of this kind would hardly be conducive to the development of paregoric addicts, if the laws and experience of human nature count for anything. What the Treasury Department has in mind is to obtain from Congress the authority to make any and all regulations it pleases for the manufacture, sale, possession, compounding, and dispensing of narcotic drugs and preparations containing them in any quantity, however negligible. If this power is vested in the department, it will proceed to permit the administering of narcotic drug and preparations containing them upon physicians' prescriptions, thus perpetuating the principal source of the narcotic evil, while denying to the public the right to purchase preparations which can not possibly become habit-forming in package form as found on the shelves of drug stores. How the proposed repeal of section 6 would improve the situation is not clear. How it would furnish additional opportunities for abuses of the use of habit-forming narcotic drugs is plain.

It should be remembered that druggists purchased opium, morphine, and similar drugs for use in making their own preparations, including paregoric, before the enactment of the Harrison act and sold them in quantities of 10 or 20 cents' worth at a time. The restrictions of the act were such, however, that they soon found it unprofitable and inadvisable to purchase these narcotic drugs. The temptation to burglars was great, as was the responsibility of druggists. They therefore changed their policy and bought narcotic preparations already prepared, so that to-day the average druggist carries in stock little or no narcotic drugs in their original state. It is not surprising, therefore, that the sales of narcotic preparations by druggists have increased 100 per cent, or more, according to the Treasury Department. If they had increased 1 000 per cent it would not necessarily mean that as much opium had been dispensed in narcotic preparations since the form of distribution was changed as was sold when druggists were making their own narcotic preparations and dispensing them in small quantities.

For the foregoing and other reasons, the statement of which the lack of time and space will not permit, your honorable committee is earnestly requested to strike out of the pending revenue bill sections 1008, 1009, and 1010. The objections entertained against sections 1008 and 1010 are based on the contention mainly that if Congress in its wisdom sees fit to amend the Harrison act, it should be done through legislation independent of revenue legislation, after careful consideration of the subject and a full and fair opportunity for the organized drug trade and pharmacy to be heard.

Very respectfully,

EUGENE C. BROCKMEYER,
General Attorney.
FRANK T. STONE,
Chairman, Legislative Committee.

NATIONAL ASSOCIATION OF RETAIL DRUGGISTS,
Washington, D. C., September 12, 1918.

THE FINANCE COMMITTEE,
United States Senate, Washington, D. C.

GENTLEMEN: The National Association of Retail Druggists, representing the more than 50,000 drug stores of the United States, asks the indulgence of your honorable committee for the privilege of submitting for your careful consideration the following in relation to the proposed tax on beverages as provided in section 630, page 115, of H. R. 12863:

The tax on soda-fountain drinks.—This provision levies "a tax of 2 cents for each 10 cents or fraction thereof of the amount paid to any person conducting a soda fountain, ice-cream parlor, or other similar place of business, for drinks commonly known as soft drinks, compounded or mixed at such place of business, or for ice cream, ice-cream sodas, sundæes, or other similar articles of food or drink, when any of the above are sold for consumption in or in proximity to such place of business: *Provided*, that in cases where the charge for any such article is 7 cents or less, the tax shall be 1 cent. Such tax shall be paid by the purchaser to the vendor and shall be collected, returned, and paid to the United States by such vendor in the same manner as provided in section 502."

Section 502 provides that vendors shall collect the tax imposed from the person making the payment of such tax and shall make monthly returns under oath in duplicate and pay the taxes so collected to the local collector of revenue.

Retail druggists have no complaint against the tax itself; they merely ask your honorable committee to readjust the rates of taxation, so that neither the revenue of the Government nor the profits of the druggist will suffer. We are entirely satisfied with the tax of 1 cent for each drink selling at a fountain or stand for 7 cents, or fraction thereof. We suggest, however, that the bill be amended so as to provide a tax of 2 cents for each drink selling for more than 7 cents and not more than 20 cents, with such additional tax for each drink selling at more than 20 cents as the good judgment of your honorable committee may dictate. Ice-cream sodas as a general thing nowadays sell for 15 cents. Under the bill as it now reads the tax on such sodas would be 4 cents, because a tax of 2 cents is imposed for each 10 cents or fraction thereof paid for a soda-fountain drink. The effect of raising the selling price of ice-cream sodas to 19 cents, including the proposed tax, would be to greatly discourage the purchase

and sale of ice-cream sodas and force the consuming public to the 5-cent drinks.

This, of course, would increase the proceeds of the Government from the 1-cent tax proposed, but would cause large loss of revenue from the 2-cent tax proposed. Aside from the consideration of revenue and the profits of retailers, which would greatly shrink under the rates proposed, the far more important consideration is the effect of the proposed rates on the public. Depriving the American people of ice cream soda—that is, a large majority of them, or those able to pay 15 cents for a drink and no more—would be unwise from two points of view: It would deprive the consuming public of the benefit of the food value of the large majority of drinks consumed at the soda fountain by forcing them to consume the 5-cent drinks containing no ice cream or milk, and would also take away from them one of their most popular luxuries and forms of diversion. The "movie" and the soda fountain have come to be the common form of entertainment and pleasure for the masses and anything which tends to discourage this form of diversion or entertainment without providing a good substitute for them would be against public policy, particularly in the hour of the Government's trials.

Your honorable committee is therefore earnestly urged to amend section 630 in accordance with the suggestions herein respectfully submitted.

In these trying times for the Government no special interest has any claim for consideration at its hands, especially where the needs of the Government for the prosecution of the war are concerned. In this instance, however, it should be remembered that the public welfare is the highest consideration. The health and life of the Nation demand adequate and efficient pharmaceutical service. Drug stores can not be operated by the sale of drugs and medicines alone because the volume and profits of such business will not maintain any drug store alone. The soda-fountain business is the largest and most profitable item of the average drug store. Many druggists depend upon the profits derived from this source in the spring, summer, and autumn seasons to tide them over the lean days of the winter. It would, indeed, be unfortunate and unwise for Congress to cripple this phase of their business while at the same time imposing a 10 per cent tax on medicines, cosmetics, and similar articles and twice the present tax on alcohol used for pharmaceutical purposes. These burdens, together with the loss of qualified help caused by the draft, will make it a serious question as to whether or not drug stores can continue as agencies for the compounding and dispensing of necessary drugs and medicines.

Very respectfully,

EUGENE C. BROKMAYER,
General Attorney.

FRANK T. STONE,
Chairman Legislative Committee.

NATIONAL ASSOCIATION OF RETAIL DRUGGISTS.
Washington, D. C., September 12, 1918.

THE FINANCE COMMITTEE,
United States Senate, Washington, D. C.

GENTLEMEN: On behalf of the more than 50,000 retail druggists of the United States the National Association of Retail Druggists has the honor to submit for your careful consideration the following brief in relation to the proposed taxation of distilled spirits for medicinal and industrial purposes and proprietary preparations in H. R. 12,863, Union Calendar No. 256:

Poor man's medicine taxed many ways.—Your honorable committee wisely and justly differentiated between medicines and cosmetics and similar articles and excluded the proposed tax on the former in the revenue act of 1914. You promptly sustained the point that medicines are necessities while cosmetics and similar articles are luxuries.

The War Industries Board recently has classified drugs and medicines as essentials and placed them on the preferred list so as to insure their continued manufacture and distribution in the interest of the health and life of the Nation.

The Ways and Means Committee of the House, however, has classified medicines and cosmetics and similar articles alike in the pending bill and imposed a consumption tax of 1 cent for each 10 cents or fraction thereof paid by the consuming public. The tax on both under the present law is 2 per cent of the manufacturer's selling price.

The national administration recommended doubling of existing taxation to meet the requirements of the war, and the pending revenue bill has been framed in accordance with that recommendation, except in the case of medicines and cosmetics and similar articles. A consumption tax of 4 per cent, therefore, would meet the needs of the Government and not prove a discrimination against a recognized necessary of life, so far as medicines are concerned.

Besides the 10 per cent tax on medicines and cosmetics and similar articles, the pending bill levies a tax of \$4.40 per proof gallon on medicinal and industrial alcohol, commonly called nonbeverage alcohol, double the present tax. This amounts to \$8.20 per gallon as used for the manufacture of medicinal preparations, because alcohol so used must be 188 per cent proof. Your honorable committee is doubtless aware that alcohol is indispensable as a solvent, preservative, or because of its therapeutic value in making medicinal preparations and is largely used for such purposes. It is estimated that the proposed tax on nonbeverage alcohol would amount to not less than 51 per cent, of the entire gross sales of a certain popular and widely used liniment during the past year, and to from 10 to 35 per cent of the gross sales of other similar preparations. Add to this a 10 per cent consumption tax and your honorable committee will perceive the extent of the additional burdens proposed for the poor man's medicine, as well as the medicine of all classes, including that manufactured for the use of the naval and military forces of the nation. Nor is this all. In addition to these specific taxes the manufacturers of drugs and medicines are required by the pending bill to pay income, war, and excess profits and the other taxes levied on manufacturers and other classes of citizens generally. Why drug and medicine manufacturers, wholesalers, and retailers should have been singled out as the subjects for so many different forms of taxation, and why the consuming public should also be discriminated against in the taxation of these necessities, is difficult to understand, if reason, justice and wise statesmanship are to be the guide of the national lawmakers. The retail druggists of the country are heartily in sympathy with the patriotic purpose of the Government and Congress to raise all revenue required for the successful prosecution of the war and are more than willing to bear their fair share, whether in the form of direct taxes, or as additional burdens imposed on them in the administration of the proposed taxes. All they ask is that there be no inequality, or discrimination, against the drug trade and pharmacy. Aside from their selfish interests, your honorable committee should not overlook the fact that alcohol is used by druggists everywhere in compounding their own preparations, as well as physicians' prescriptions, so that druggists are quite as much interested in the proposed excessive tax on nonbeverage alcohol as the large drug and pharmaceutical manufacturers. What is more, druggists are manufacturers of preparations included in paragraph (h) of section 800 of the revenue act of 1917 which the pending bill designates as the subject of 1 cent for each 10 cents, or fraction thereof, of the retail price, a consumption tax, but none the less a tax on the time and labor of the druggists in the collection and return of the tax. Consequently druggists are no less concerned, or affected, by this proposed tax than the large drug and pharmaceutical manufacturers; nor is the consuming public less affected by it, so far as the selling price of medicinal preparations is concerned. The danger is that the selling price of necessary drugs and medicines to the public will become prohibitive if your honorable committee should retain the rates of taxation proposed on proprietary preparations and nonbeverage alcohol in the pending bill. In addition to reducing the proposed tax to 4 per cent on proprietary preparations, this association respectfully urges your honorable committee to specifically designate that the tax be a stamp tax and that it be collected from the purchaser by the retailer at the time of sale in the form of a stamp canceled and affixed by the retailer.

The pending bill authorizes the Commissioner of Internal Revenue to collect this tax either by the method just suggested or by requiring the purchaser to pay the tax to the vendor and compelling the vendor to make monthly returns under oath in duplicate and pay the taxes collected to the local revenue collector. The latter method would have the effect of requiring druggists to keep so many records in addition to those they are now required to keep by other branches of the Government that it would be most difficult for the drug stores of the country to continue in operation, particularly with the shortage of registered pharmacists now prevailing, which promises to become even more serious under the operation of the new draft law. Eighteen drug stores have been closed in the District of Columbia alone during the past six months on account

of the shortage of help and difficulty in obtaining necessary supplies, and for other reasons. This represents 7.4 per cent of the total number of drug stores in existence six month ago. It is predicted that there will not be less than 50 additional drug stores closed within the next three months under the new draft law, because of the shortage of qualified and registered pharmacists. Therefore, your honorable committee will observe that the public welfare is directly affected by the excessive burdens proposed in the pending bill, which, although of a revenue character, are none the less calculated to make it difficult or impossible to continue drug stores in operation and thus jeopardize the health and life of the Nation, so far as the public depends upon drug stores for the compounding of prescriptions and dispensing of necessary drugs and medicines. Still another provision of the pending bill is calculated to drive drug stores out of business. Section 908 provides that "a tax of 1 cent for each 10 cents or fraction of the amount paid" for any of the articles taxed when sold for consumption or use shall be paid by the consumer. This language should be changed so as to provide that the tax imposed finally—4 per cent it is to be hoped—shall be based on the price stamped upon them by the original manufacturer, and in cases where articles subject to the tax have no price stamped upon them, the tax be based upon the ordinary and accepted value of such articles, the method adopted by the Internal Revenue Department in the collection of the war tax during the Spanish American War. The objection to the language in the pending bill is that it will greatly encourage predatory price cutting. This will not only drive drug stores out of business by making it impossible for them to compete with department store and other price cutters, who cut the prices of some standard article and advertise it as a bait for the attraction of unwary purchasers whom they fleece through the sale of other articles at exorbitant prices, but will also have the effect of driving off the market articles of established and known value and the substitution therefor of articles of inferior quality selling for far more than they are really worth.

In passing your honorable committee will note that the pending bill imposes other burdens on retail druggists, including the obligation to collect, return, and pay the tax imposed on every drink sold at their soda fountains. This association does not complain, merely calling the attention of your honorable committee to the practical difficulties confronting the pharmacist in continuing the operation of the average drug store and rendering efficient, safe, and necessary pharmaceutical service indispensable to the health and life of the Nation.

Very respectfully,

EUGENE C. BROCKMEYER,
General Attorney.

FRANK T. STONE,
Chairman Legislative Committee.

(The following brief was subsequently submitted to the committee by Mr. Charles M. Woodruff, and by order of the chairman is here printed in full, as follows:)

STATEMENT ON BEHALF OF MANUFACTURING PHARMACY RESPECTING THE WAR-REVENUE BILL OF 1918, KNOWN AS H. R. 12863.

SUMMARY.

- I. A protest against the increased tax on nonbeverage alcohol.
- II. A suggested provision to be added to section 908, paragraph (a), to make the legislative intent more certain.
- III. A plea for a better opportunity to consider the rider amending the so-called Harrison Act (secs. 1008, 1009, and 1010) than can be afforded in connection with this revenue bill.

"Drugs and medicines" have been formally recognized by the War Industries Board as essential to the welfare of both the civilian and the military population. No attempt has been made to distinguish between schools of practice or opposing opinions of medical men, it having been recognized that the public and the medical profession as a whole must be treated on the basis of equality before the law.

Moreover, it has been recognized that the neighborhood drug store, as the immediate point of contact with the public, is an essential to the health of the country as the family physician; and that very few drug stores could exist if it failed to supply the medical needs of the whole community.

Few, indeed, do not depend in some degree upon the doctor, who may be a "regular," "eclectic," or "homeopath." Even among "regulars" there are opposing views as to the most effective form of medicament, and the value of particular drugs—the result being that any list likely to meet the requirements of the profession as a whole must provide several times as many preparations as have been "recognized" by those who have compiled the so-called "official" formularies.

Manufacturing pharmacy must therefore perform its functions with the same impartiality as those who have to do with the enactment, the administration, and the enforcement of law. It is its function to reduce the crude drug to that form of medicinal preparation that will make it efficient and available to the physician whose experience and observation leads him to prescribe it.

Not considering modern serum therapy, the crude source of all but a very few prepared substances is botanic in character. Herbs, roots, barks, flowers, leaves, and sometimes whole plants contain certain active principles which it is the province of manufacturing pharmacy to isolate from the mass of inert matter confining them, and present in a form that will insure permanency and efficiency, certainty of dosage, and other advantages not necessary to name.

To this end some extractive agent or solvent must be employed that will bring away the desired active principle. In 90 cases out of every 100 this extractive agent or solvent is alcohol. Pharmaceutical science knows no other.

The manufacturing pharmacist therefore does not use alcohol from choice, but because he is obliged to. Find him an efficient substitute and he will gladly adopt it.

The tax on alcohol is already higher than is just. It is many times the value of the article itself. No other industrial requisite is so severely taxed, and but few are taxed at all. In looking for more revenue why not leave alcohol as it is under the law of 1917 and levy a tax upon one or more substances that are now unburdened by any tax?

The enormity of the tax upon alcohol does not fully appear until it is reduced to terms of wine gallons. The war-revenue law of 1917 doubled the existing tax on industrial alcohol, and made it \$2.20 per proof gallon, or \$4.14 per wine gallon, figuring alcohol at 188 proof. The present law doubles this and makes the tax \$4.40 per proof gallon, or \$8.28 per wine gallon.

The seriousness of this enormous tax might be more fully realized if time had permitted a canvass of those engaged in this essential industry that would have afforded a summary of the experience of the industry as a whole. As it is, it may be said that one concern alone will have to pay more than \$900,000 per year based on its consumption for 1917. How many concerns can meet this extra tax without embarrassment? And yet all must meet it in some way or fall in their duty to the public as manufacturing pharmacists.

It may be suggested that the manufacturer can pass the tax along; but an emergency tax, such as the proposed, is an uncertain element of cost and renders the business affected by it extremely hazardous. What may be gained at one end will be more than lost at the other. By an unchangeable law of economics prices of stocks on hand must be such as will protect against loss when the tax is repealed, and goods manufactured under it must be sold at less than the cost of production.

This inevitable disturbance of an important industry at two critical periods, now and when the readjustment comes, is a strong argument against this unjust alcohol tax.

The tax on beverage alcohol affects the industry and trade in this way: Under the present rules and regulations, before a manufacturer can use industrial alcohol for any purpose, he must file a bond in a penal sum equal to three times the difference between the tax on nonbeverage alcohol and beverage alcohol multiplied by the number of gallons he expects to have on hand or in transit at any one time. This amount is relatively large. It is not practicable, under present regulations, to file a personal bond, and the bonding companies are combined as to premium required for such bonds, which is very high—based on the theory that those engaged in this essential industry and trade are potential criminals.

Finally, the proposed measure entails upon the producer of the drugs and medicines so essential to the health and welfare of the public the obligation to pay on whatever stock of alcohol he may have on hand when it goes into effect the sum of \$2.20 per proof gallon, or \$4.14 per wine gallon. This will amount to more than many manufacturers will have in bank and will involve the necessity of borrowing. In some cases it will doubtless cause some degree of

financial embarrassment; in all cases it will be unjust imposition upon an essential industry not compensated by the returns.

It is therefore requested on behalf of manufacturing pharmacy that the war-revenue act of 1918 do not increase the tax imposed upon alcohol by the war-revenue act of 1917.

THE TAX ON PERFUMES, TOILET PREPARATIONS, AND PATENT MEDICINES.

The context and the use of the words "consumption or use" in sections immediately preceding section 908, paragraph (a), would seem to make the "legislative intent" very clear. It unquestionably has reference to the final sale across the retailer's counter, or any sale that is equivalent, as a sale by a mail-order house. In one sense these terms are synonymous, and the last purchaser is the ultimate consumer, whether he eats it or whether he wears or otherwise uses it, so that its identity remains unchanged indefinitely.

It is not thought that it is intended to tax the manufacturer who purchases an article included in the enumeration for the purpose of producing another article, or the physician to pay a tax upon the medicine he administers in convenient doses but does not charge for specifically, or the druggist to pay a tax on the many products he buys to dispense upon physicians' prescriptions and orders, or the patient upon the mixture his physician has prescribed for him. And yet these practical (administrative) interpretations are likely to be made, and if long continued and acquiesced in may be finally confirmed by judicial construction.

Therefore, believing it does not change the intent of Congress, but makes it more clear, it is asked that the following provision be inserted at the end of paragraph (a), section 908:

"Provided, That any article sold for use in manufacturing any other article intended for sale for consumption or use, and any article sold to any regular pharmacist for use in compounding prescriptions, or any article sold to any physician or hospital for administration to any person being treated by such physician in such hospital, or any article sold to a dentist or veterinarian for use in his practice, shall not be considered as sold for consumption or use within the meaning of this section unless a charge is made for such article apart from the fee charged by such pharmacist, physician, hospital, dentist, or veterinarian for professional services, in which case such pharmacist, physician, dentist, or veterinarian shall be regarded as the vendor under paragraph (b) of this section."

WHY THE AMENDMENTS TO THE SO-CALLED HARRISON ACT SHOULD NOT BE CONSIDERED IN CONNECTION WITH THIS BILL.

Sections 1008, 1009, and 1010 of the bill now under discussion comprise two measures originally introduced by Hon. Henry T. Rainey as H. R. 9830 and H. R. 12787.

Section 1010 (H. R. 9830) respects the disposition of opium, etc., under seizure by the United States Government and happens to be exactly in harmony with a resolution adopted by the American Drug Manufacturers Association.

Sections 1008 and 1009 make radical amendments to the so-called Harrison antinarcotic act.

This act was the result of the combined efforts of Dr. Hamilton Wright and the entire drug trade of the country represented by the National Drug Trade Conference to agree upon a measure that would prevent the police laws of the several States affecting narcotics from being nullified by the natural operations of commerce between the States. There were efficient laws to prevent habitues from securing supplies in their own States; but none to hinder them from purchasing across the border. Bills which had been introduced were opposed by the trade as unnecessarily burdensome and unworkable. Since manufacturers were obliged to produce preparations of the inhibited articles in their capacity as suppliers of the doctor's requirements, and dealers by the same token were required to distribute them, as well as physicians to prescribe them; and since all were in favor of workable restrictive measures, the right of their accredited representatives to be consulted in the working out of a practical measure was conceded, and the work of the National Drug Trade Conference was commended by Representatives Harrison, Manna, and others when the bill was introduced in the House; and by Senator Thomas when it came up in the Senate.

In May, 1917, a conference was held under the auspices of the National Drug Trade Conference, to which came representatives from several States, duly appointed by governors, mayors, and other officials, to exchange experiences and determine what amendments to the act were needed to make it more effective.

It is not the purpose of this protest to speak of the merits of the amendments to the Harrison Act. It is enough to know that they are important and should be considered apart from the war-revenue act to which they have been attached as a rider; and that the National Drug Trade Conference, which meets soon, should have the opportunity of a hearing after first considering the measure in deliberative assembly as a separate feature.

A protest against this method of rushing through an important measure to which one faction is committed reflects only upon a system which has prevailed altogether too long in Federal legislation. It is a method provided against by the constitutions of most of our States, and, if the writer does not misrecollect, decried by our esteemed President.

All that is asked in this connection is that sections 1008, 1009, and 1010 may be stricken out of the war-revenue bill, to be reintroduced as a separate measure for more deliberative consideration than can be given it in this connection.

The necessity of this action is illustrated by the stamp-tax feature under which cocaine is taxed no more per ounce than coca leaves, notwithstanding an ounce of cocaine represents many pounds of coca leaves.

One ounce of opium is taxed as much as one ounce of morphine, which represents many ounces of opium.

Then when it comes to compounds and preparations we have this anomaly: The less of cocaine, for example, a mixture contains the higher the tax per ounce of cocaine.

A package containing one ounce of cocaine is taxed 1 cent.

A mixture representing one-eighth grain cocaine to the fluid ounce would be taxed at the rate of 16 cents per pint bottle, representing 2 grains of cocaine—equivalent to a tax of 8 cents per grain of cocaine, or \$35 per ounce.

A provision levying a minimum stamp tax of 1 cent per single package, and basing the tax on the ounce or fraction thereof of cocaine or its salts, or of morphine or its salts, etc., represented in the mixture would prevent such an anomaly.

Protestations of loyalty are in bad taste. Everyone and every interest is presumed to be loyal. There may be differences of judgment, variations of opinion, and equally sincere patriots may be wide apart respecting the wisdom of particular plans; but all true Americans are one in wishing for a complete victory over the most brutal and potent foe our Nation ever contended against; and we are all one in our willingness to sacrifice whatever may be necessary to this desired end. The situation, however, does not justify injustice to any interest nor wrong to an industry so important to the health of our people as is manufacturing pharmacy.

Respectfully submitted,

CHARLES M. WOODRUFF,

Counsel for the American Drug Manufacturers' Association.

DETROIT, MICH.,

September 14, 1918.

PROTEST FROM MICHIGAN MANUFACTURERS.

DETROIT, MICH., September 14, 1918.

To the Michigan Delegation in Congress.

HONORABLE SIRS: A meeting of representatives of the retail drug trade and leading jobbers and manufacturers of pharmaceutical preparations of Michigan met at the board of commerce in Detroit, Mich., Friday noon, September 13, 1918, for the purpose of considering those features of the pending revenue bill (H. R. 12863) peculiarly affecting the manufacture and sale of drugs and medicines.

After full discussion the acting chairman of the meeting was unanimously instructed to send a copy of the following protest to the Senators and Congressmen from Michigan:

"Protest is respectfully made against the increase on the tax on alcohol necessarily used for extractive, solvent, and preservative purposes in the production of medicines.

"Our experience leads us to believe that the large increase in revenue estimated by the committee will not materialize as the result of the increased tax. Manufacturers are likely to suspend further production of many necessary fluid preparations, leaving the public and the medical profession to depend upon present stocks for supplies. The result will be that the drug trade will be put to the inconvenience and expense entailed by this very material increase in tax without any marked compensating increase in revenue to the Government.

"Under the operation of Title VI the drug trade will first be obliged to pay a very large sum in the floor tax provided for in section 604. In many cases the assessment will be more than the retailer, the jobber, or even the small manufacturer can meet without embarrassment, considering the stringency of the money market and other conditions vitally affecting the conduct of the business, which is certainly not overcapitalized.

"Drugs and medicines are necessities both to the civilian and our military population, and have been so recognized by the War Industries Board. The immediate contact between the drug and medicine industry is the neighborhood pharmacist, who is now struggling with natural and created conditions involving high cost of supplies, shortage of help, an intricate amount of detail in complying with State and national pharmacy laws, poison laws, liquor laws, etc., and it is certainly unjust and unfair to an industry and trade recognized as so important to impose upon it the increased alcohol tax in addition to the heavy burdens which the industry and trade must bear under the act in common with all other industries and trades. We therefore respectfully petition that there be no increase in the alcohol tax over that imposed by the revenue act of 1917. Before leaving this subject we would respectfully point out that the beverage tax may not seem to affect the drug trade in Michigan because of the State's prohibition law, but the regulations require all handling nonbeverage alcohol for any purpose to have a permit from the Commissioner of Internal Revenue which shall be based upon a bond the penalty sum of which is fixed on the difference between the nonbeverage alcohol tax and the beverage alcohol tax. The beverage alcohol tax, of course, is prohibitive. It is \$8 per proof gallon (approximately \$16 per wine gallon). The requirements of the revenue department have been such as to make it practically impossible to file a bond with personal sureties, and the insurance companies recognized by the department have taken advantage of the monopoly they enjoy to charge a very high rate of premium."

At this meeting it was determined to ask no change in section 630, imposing a tax upon soda fountain drinks, etc., and making the druggist the collector of this tax, although it seriously embarrasses him with respect to reports because of the present shortage of competent help.

The meeting also expressed itself as satisfied with the provisions of section 908 for the collection of the tax on perfumes, toilet preparations, and certain medicinal preparations; but to avoid any possible misconstruction of the intent of Congress as well as to prevent a tax upon the sick under the care of physicians, etc., which would result from such misinterpretation, the meeting resolved to ask that a provision be inserted which would make it clear that the tax should not be imposed upon prescriptions, upon supplies furnished physicians for the treatment of the sick, to veterinarians likewise, and also to dentists for use in dental operations. We therefore suggest that some such phrase as the following be inserted after the words "sold for consumption or use" in the first paragraph of section 908: "*Provided*, That the dispensing of any article mentioned in paragraph (2) upon physicians' prescriptions written in good faith, or the bona fide sale of any such article to physicians, veterinarians, and dentists to be used in their medical and dental practice and operations, shall not be considered as sold for consumption or use."

It was finally concluded by the meeting referred to above to ask the elimination of sections 1008, 1009, and 1010, for the reason that these sections involve important amendments to the Harrison Act which should be considered apart from the war-revenue bill. The meeting did not wish to commit itself on these amendments, but did feel that a fuller opportunity should be given for their consideration than is afforded in this connection; therefore that the bill originally introduced by Mr. Rainey and incorporated in the war-revenue bill should be reintroduced, referred to the proper committee, and an opportunity be given to the various branches of the trade and the medical profession for a hearing upon the same.

For the present, therefore, the objection of those represented at the meeting is to the method of enactment rather than to the features of the proposed

measure itself. It is not necessary to say more than that such method is inhibited by constitutional provisions in the constitution of Michigan and in many, if not most, of the several States of the United States of America.

Manufacturers and dealers in drugs and medicines do not handle the substances and preparations coming under the operation of this law from choice, but from necessity, and in the performance of their functions as suppliers to the medical profession of those therapeutic agents required by that great profession in the treatment of the sick.

They therefore feel that, inasmuch as they were consulted through the National Drug Trade Conference with respect to the original act, they should have an opportunity of considering these important amendments in a more deliberative way than is now possible.

All of which is respectfully submitted.

JOHN H. WEBSTER, *Chairman.*

The CHAIRMAN. Senator Kellogg has asked the committee to hear this evening, if possible, Mr. Zollman or Gen. Crowe.

STATEMENT OF MR. F. W. ZOLLMAN.

Mr. ZOLLMAN. Mr. Chairman and gentlemen, I represent the manufacturers of cereal beverages in the State of Minnesota, Gen. C. E. Crowe, of St. Louis, represents them in Missouri, and Mr. W. H. Austin, of Milwaukee, who will be here in a few moments, represents the same manufacturers in the State of Wisconsin.

Senator ROBINSON. What manufacturers?

Mr. ZOLLMAN. The manufacturers of cereal beverages that are covered by section 628 of the revenue bill, which imposes a tax upon all beverages—soft drinks.

The CHAIRMAN. And near beer?

Mr. ZOLLMAN. Near beer and all other soft drinks.

We appear before this committee for the purpose of asking that section 628 be amended so that the tax which it is proposed to place upon these beverages shall not be imposed upon the containers in which they are sold.

Senator PENROSE. What kind of containers are they sold in?

Mr. ZOLLMAN. In bottles, in cases, and in casks. The reason we make this request is because we have found it necessary to make a charge for these containers and to add that charge to the price of the beverage on our books or in the invoices to the parties to whom the beverage is sold.

That course of business was necessary in order to insure us against the loss of these containers, to insure payment for them in case they were returned, and to see that they are returned.

A little history here probably would explain the situation and give you a concrete example of just how we arrived at that conclusion. Formerly no charge was made at all for bottles or cases, and that is what we call a container or package. We call them package charges up our way, but many of them call them containers. We made no charges for packages at all.

As competition grew, the packages were not returned, and that involved an immense loss in bottles and in cases.

The next step in order to protect the business was to make a charge for packages or containers, and we made a separate charge, or what is known as a memorandum charge—that is, we separated the two and the beverage was charged separately and the package separately,

but all on one book, a separate item for each, the package charge being merely a memorandum charge.

We found that that did not bring results, because at the end of the week or the month, as the case might be, the consumer simply remitted the actual beverage price. The fact that the beverage price was separated from the package price emphasized the separation and the distinction, and the consumer acted, in the payment of his bill, upon that distinction.

We found that the loss was so enormous that we could not do business that way, because the package cost us fully one-half, if not more than one-half, of the beverage price, or rather, the cost of the beverage; so that we then jointed the two charges—that is, the charge for packages was added to the beverage price and so entered upon the books and billed so upon the invoice, so that there was no distinction whatever made between the two items. This produced results, because it induced the purchasers to return the packages, and if he returned them he was given credit for them upon our books. If he did not return them, the charge was made and it was collected from him. That was the reason, as I say, for adopting this charge and making it in that way. We have drafted an amendment here which we believe covers the situation, and I will read it with the permission of the committee [reading]:

Amend H. R. 12863 by striking out of line three (3) of section 628, the words, "so sold," and insert after the word, "price" in line three (3) of section 628, the following, "for which the beverage itself is sold, exclusive of any sum charged in the invoice of the sale for closed or other containers," so that said section will read as follows:

"Sec. 628. That there shall be levied, assessed, collected, and paid in lieu of the taxes imposed by sections 313 and 315 of the Revenue Act of Nineteen Hundred and Seventeen—

"(a) Upon all beverages derived wholly or in part from cereals or substitutes therefor, and containing less than one-half per centum of alcohol, sold by the manufacturer, producer, or importer, in bottles or other closed containers, a tax equivalent to thirty per centum of the price for which the beverage itself is sold, exclusive of any sum charged in the invoice of the sale for closed or other containers, and upon all unfermented grape juice, ginger ale, root beer, sarsaparilla, pop, artificial mineral waters (carbonated or not carbonated), other carbonated waters or beverages, and other soft drinks, sold by manufacturer, producer, or importer, in bottles or other closed containers, a tax equivalent to twenty per centum of the price for which so sold; and

"(b) Upon all natural mineral waters or table waters, sold by the producer, bottler, or importer thereof, in bottles or other closed containers, at over ten cents per gallon, a tax of two cents per gallon."

The only change that is made there, as I said before, is in the language "for which the beverage itself is sold, exclusive of any sum charged in the invoice of the sale for closed or other containers."

The CHAIRMAN. Let me ask you, would there not be an opportunity created by that amendment to price the beverage at a minimum price and the container at a maximum?

Mr. ZOLLMAN. I think not.

The CHAIRMAN. Why not?

Senator SMOOT. That could be done.

The CHAIRMAN. Why could it not be easily done?

Mr. ZOLLMAN. The sale price is easily known, and there is a record kept of that, and our package price is well enough known. Even if the packages were included, if this amendment were rejected, some people charge less than we do in Minnesota; the price varies. Some

charge \$1.20, some charge 90 cents, and some \$1.30. The matter of evasion of the law would be just as apt to be sought, if there were a disposition to seek it, as it would by amending this law so that no tax charge could be placed upon the container.

SENATOR McCUMBER. But in those cases are not the charges made for the containers sufficient to make a profit upon the containers themselves?

Mr. ZOLLMAN. Oh, no. The charge which is made for the containers in most instances does not cover their cost. For instance, we used to buy cases at 75 cents and 85 cents. They cost us \$1.25 now, and independent of the bottles, the charge which we make, that is the charge of \$1.50, which is made in the State of Minnesota, does not cover the cost of the container.

Senator McCUMBER. You mean to say, then, if one charges 90 cents and the other \$1.25 for the container, the man who charged 90 cents is charging less than the cost?

Mr. ZOLLMAN. He certainly would be charging less than the cost of the container. This charge, Senator, is made simply to give us some protection against their loss.

Senator SMOOT. And to insure their return?

Mr. ZOLLMAN. To insure their return; or if they are lost to insure payment on the part of the person who loses them. You can readily see that if we were obliged to pay a tax upon the containers, we would pay that tax every time they were returned and reused and sent out again, and we might pay tax upon those containers ad infinitum. The only addition made here is in the words "or other containers," and the only reason we use the words "other containers" in this amendment is this. In the shipping business, or where it is sent out away from the place where it is manufactured, these containers or cases have a lid on them and are closed. For the local business most of the cases have no lids whatever, but the bottles are simply placed in them, in which the beverage is contained. And we are not objecting to any tax; it is not a question of the amount of tax levied here, but it is a question of taxing so far as there might be a construction in connection with the language of this act to place or impose a tax upon the containers themselves, and I think that construction is liable to be made, because the original bill says, "in bottles or other closed containers;" and as I said before, the price at which the package of this kind now sells, including the beverage itself, as well as the price at which a beverage of this kind now sells, includes the beverage itself as well as the container. No distinction is made.

The CHAIRMAN. Will you file your amendment?

Mr. ZOLLMAN. Yes, I will file that. I do not know but that Gen. Crowe will have some suggestions to make, which will bear on this situation somewhat, if the committee desires to hear him.

The CHAIRMAN. Is Gen. Crowe present?

Gen. CROWE. Yes, sir; I do not desire to take the time of the committee.

The CHAIRMAN. Mr. Marston, we will hear you now. State your name to the stenographer.

STATEMENT OF MR. J. FREEMAN MARSTON, PRESIDENT OF THE TAXI SERVICE CO., OF BOSTON, REPRESENTING THE TAXICAB INTERESTS OF NEW ENGLAND.

Mr. MARSTON. Mr. Chairman and gentlemen, paragraph 12 of section 1001 of the War Revenue bill, as reported by the committee on Ways and Means, provides "that every person carrying on the business of operating for hire three or more passenger automobiles shall pay a tax of 5 per cent on the gross receipts during the preceding year ending June thirtieth, from the operation of each such automobile."

That seems to be a tax which the Taxi Service Co., the largest Taxicab Co. in New England, would find it very difficult, if not impossible, to pay. For the last eight years the net profits of our company in no one year have equaled five per cent of the gross receipts.

Senator PENROSE. Which is your company?

Mr. MARSTON. The Taxi Service Co., of Boston.

Senator SMOOT. How many taxies have you?

Mr. MARSTON. We operate slightly over two hundred.

Senator SMOOT. How many are therein Boston?

Mr. MARSTON. There are about two thousand.

Senator SMOOT. The law provides that the two hundred shall be taxed and the rest of the two thousand shall be exempt?

Mr. MARSTON. You took the words out of my mouth, Senator. That is just the point. The provides for that tax on the gross receipts of our company, but applies no tax whatsoever on all independents, the so-called "skimmers" as we call them, who have one car, and drive that.

In addition to this tax of 5 per cent on the gross receipts, we will be, under this bill, compelled to pay a tax of 2 cents a gallon on gasoline, thereby increasing our cost by 2 cents.

Senator THOMAS (in the chair). What is the difference between the cost to the customer dealing with your company and dealing with the independent taxicab man?

Mr. MARSTON. No difference whatever, excepting that our charge is set by ordinance, and we are a reputable corporation and a person can come back to us, or to one of the hotels from which we run, whereas it is difficult to come back and find the "skinner."

Senator SMOOT. In other words, these "skimmers" that run from 12 o'clock at night until 4 o'clock in the morning and rob everybody they can get their hands on?

Senator THOMAS. The Senator speaks feelingly.

Senator SMOOT (continuing). They are to escape taxation?

Mr. MARSTON. Yes, sir.

Senator LODGE. Out of 2,000 taxicabs in Boston, under this provision which exempts anyone who owns less than two, 1,600 would escape, because there are only 400 which are operated by companies?

Mr. MARSTON. Yes, sir.

Senator PENROSE. Did you present your views to the Ways and Means Committee?

Mr. MARSTON. No, sir, we did not. The first I knew of this was from the Boston News Bureau, when I saw the story that at the last

moment a tax of 2 per cent on the gross receipts of the taxicab companies was written into the bill.

In addition to this 2 per cent we have to pay 2 cents a gallon on gasoline. We have to pay an excise tax which ranges from \$10 to \$50 per car, according to the horsepower of the automobile. We operate 20 twin-six Packard cars, which would be taxed for the \$50 amount, which makes \$1,000 there, and slightly over one hundred and fifty taxicabs which would be taxed at \$40 apiece, making \$7,000 of taxes on our taxicabs and touring cars.

Senator SMOOT. The tax is general?

Mr. MARSTON. Yes, the tax is general, and we are not finding any fault with that. We are taxed 10 per cent on all tires, accessories and parts that go into the upkeep of an automobile, which we will gladly pay.

Senator SMOOT. That is general?

Mr. MARSTON. That is general.

Senator PENROSE. And in addition to that you are out of business on Sundays?

Mr. MARSTON. In addition to that we are out of business on Sundays. You are quite right, Senator.

Senator PENROSE. And you have an income tax?

Mr. MARSTON. Yes; and I presume the income tax and excess-profits tax, if there are any excess profits to tax. Very briefly, I do not believe that any man that considers himself a patriot ought to come down here and appear before you gentlemen and ask to have any tax taken off. I do not ask that. All I want to do is to do what the railroads do, to add that to our tariff. We will willingly collect that tax, and we will show this committee where they can get more revenue. For example, 5 per cent of the gross receipts is 5 cents on every dollar, is it not? Well, we will collect 5 cents on every taxicab ride; and the records show that the fare for the average taxicab ride is 80 cents.

The CHAIRMAN. In other words, you will pass it on to the poor devil who rides?

Mr. MARSTON. We have got to.

Senator PENROSE. If you do not, the sheriff will get you.

Mr. MARSTON. Yes; if we do not, the sheriff will get us.

Senator SMOOT. Remember that you can eat white bread, anyway.

Mr. MARSTON. Yes; that is one consolation.

Senator SMOOT. Personally, I think your complaint about the discriminatory character of the tax is unanswerable.

Mr. MARSTON. Well, it seems to be that way, but I admit I am prejudiced. Another point is what seems to be a retroactive feature in the tax. Our lawyers can not seem to quite understand this wording. The bill provides in section 1001 [reading]:

Every person carrying on the business of operating for hire three or more passenger automobiles (other than sightseeing automobiles having a seating capacity of more than seven) shall pay a tax equivalent to 5 per centum of the gross receipts during the preceding year ending June 30 from the operation of each automobile.

Nobody seems to know what that means, "during the preceding year ending June 30." Nobody seems to be able to understand that. It has been suggested by our counsel that it means the year from

June 30, 1917, to June 30, 1918, in which case it would be retroactive one year plus perhaps three months in addition to that, and I do not know what would happen in that case, really. What that language means we have been unable to find out.

Senator ROBINSON. It means the year that ended June 30, 1918. That language is as clear as you can make it, although I do not know the necessity for expressing it that way.

Senator LODGE. It is retroactive.

Senator ROBINSON. Certainly it is retroactive. The year preceding June 30, 1918, is certainly the year ending June 30, 1918, and it would make it retroactive.

Mr. MARSTON. But they do not assess and collect it until after January 1?

Senator ROBINSON. No.

Mr. MARSTON. I see. The only other point in it is that paragraph 11 of that same book. You gentlemen will have the book open. It says:

Persons carrying on the business of operating sightseeing automobiles shall pay a tax equivalent to 10 per centum of the gross receipts.

and so on. Now, it looks as if they had it in for sightseeing automobiles more than for taxicabs, but here is a point. The prices charged by the sightseeing automobiles are not regulated by law but merely by competition, so that your sightseeing automobile which is charging \$1 for taking you around will simply charge you \$1.10 or \$1.60, or whatever the rate is. In Boston and every other large city, our taxicab rates are set by city ordinance. We are obliged to go before the police commissioners in Boston and ask for any additional rates, and it is rather unlikely that we would get any addition on rates, for it has been tried before, and our rates in Boston at present as compared with other cities in the country are high, and yet we have not been able to make any money.

Senator ROBINSON. Your suggestion is that an additional charge be made or a tax be fixed on each ride?

Mr. MARSTON. Exctly. When you buy a railroad ticket the tax is put right onto the railroad ticket if you buy at the ticket office, or if you pay to the conductor he collects the tax right there. We are in the position where we can collect a tax. When a man takes a taxicab from the South Street Station to the Hotel Touraine the driver says "Forty cents war tax."

Senator ROBINSON. You made a statement in the beginning which interested me, to the effect that it would be a physical impossibility for you to pay the tax that the bill would impose, for the reason that your net income does not equal 5 per cent of your gross income.

Senator SMOOT. Your net gain?

Senator ROBINSON. Yes; your net receipts do not equal 5 per cent of the gross income.

Mr. MARSTON. In other words, our gross receipts have been very constant, and in the last eight years they have averaged \$500,000 a year. The company has never succeeded in making \$25,000 in profits in any one year since its organization.

Senator SMOOT. You suggested that it be made 5 cents per ride. That would be hardly fair, would it, to make that charge on the trip from the depot, where there is a 60-cent charge, as compared with

the same charge for a person taking a taxicab for an extended pleasure ride and paying \$10 or \$12 for it?

Mr. MARSTON. I modified that. I have said in my brief:

If the law provided that in addition to the legal rate of fare there should be a tax of 5 cents on each ride where the fare was \$1 or less, to be paid by the passenger, and an additional 5 cents for each additional dollar or fraction thereof, the amount of revenue would be far greater than under the present proposed law.

Senator SMOOR. I did not hear the proposed amendment read or hear what you said.

Mr. MARSTON. I did not finish that. The average ride was 80 cents, I said, as our records show, and I think for a longer ride the higher tax would naturally be very proper.

Senator LODGE. The amount of that tax would undoubtedly be collected by your company and other companies, but from these individual cabs it would be almost impossible to collect it, would it not?

Mr. MARSTON. My answer to that, Senator Lodge, is this: Under the present bill there is no attempt to tax the individual cab.

Senator LODGE. None whatever; no.

Mr. MARSTON. None whatever. Therefore, if there is no tax levied upon the individual cab none will be collected.

Senator LODGE. Under your proposition you can collect a good deal from them?

Mr. MARSTON. You can collect a good deal from the individual, and you can collect it all from the corporation, and in addition to that you can collect more from the corporation, because as I showed here, all that they ask is 5 per cent of the gross receipts, which is 5 cents on the dollar. Our average ride is 80 cents, which under this bill would give 4 cents, and we would get 5 cents on every ride up to a dollar, and 10 cents from \$1 to \$2.

The CHAIRMAN. I think we understand the situation pretty well, sir.

Mr. MARSTON. Thank you, gentlemen, very much for the time.

(Mr. Marston submitted a brief which is here printed in full, as follows:)

BRIEF PRESENTED BY J. FREEMAN MARSTON, PRESIDENT OF THE TAXI SERVICE CO. OF BOSTON.

Paragraph 12 of section 1001 of the war revenue bill, as reported by the Committee on Ways and Means, provides that every person carrying on the business of operating for hire three or more passenger automobiles shall pay a tax of 5 per cent on the gross receipts during the preceding year ending June 30, from the operation of each such automobile (p. 143).

This is one of the special taxes imposed under section 1001, which provides that on and after January 1, 1919, there shall be levied, collected, and paid, annually, in lieu of the taxes imposed by section 407 of the revenue act of 1916, certain special taxes on trades and occupations. These taxes are all at flat rates, ranging from \$10 to \$1,000 annually, except in the case of persons operating sight-seeing automobiles or passenger automobiles, in which cases the tax is 10 per cent of the gross receipts in the case of sight-seeing automobiles, and, as already mentioned, 5 per cent of the gross receipts in case of passenger automobiles.

Section 14 imposes a special tax on all trades, businesses and professions, the gross receipts of which, for the preceding year ending June 30 exceed \$2,000. In such cases the annual tax is \$10, and if such gross receipts from sources other than sales directly to the consumer exceed \$100,000, the proprietor shall pay \$15 additional. In the case of mail-order houses, however, there is

a tax of 1 per cent of the gross receipts over \$100,000. With this exception the business of operating sight-seeing automobiles and three or more passenger automobiles for hire are singled out from all the businesses in the country as a subject for a tax on total gross receipts.

The rates of nearly all taxi cabs are regulated by the cities in which they operate, and therefore, such companies have no opportunity of increasing their rates so as to provide for this additional tax. Moreover, as the first tax year apparently begins June 30, 1917, even if the companies were able to secure an increase of rates to cover the new tax, no provision could be made for the tax on receipts for the period between June 30, 1917, and the time when such new rates would go into effect. This highly retroactive feature of the tax is, in itself, a strong ground of objection to a heavy tax on gross receipts.

The law also discriminates between transportation in taxicabs and transportation by rail or water, as section 500 of the act in question, imposing taxes on amounts paid for transportation of freight and passengers by rail and water, expressly provides that the taxes shall be paid by the person paying for the services or facilities rendered. In the case of persons operating sight-seeing automobiles, or conducting a mail-order business, the new taxes can be met by increasing rates; but in the case of companies operating taxicabs subject to strict regulation of rates, no such opportunity is available.

It is a well-known fact that the taxicab business, especially in the larger cities, has been a business in which a very large percentage of failures has occurred, and in which the successful companies have earned only a very modest return on the capital invested. This statement would be certainly verified by an examination of the income-tax returns of such companies. An examination of such returns would also, we venture to say, absolutely prove that the imposing of such a tax would practically ruin every person and company operating taxicabs in the larger cities in this country. According to the newspaper reports the chairman of the Ways and Means Committee, in introducing the bill to the House, expressly stated that the bill had been drawn to avoid such a result in any case. The chairman is also reported to have stated that one of the basic principles on which the act was drawn was the placing of the burden of taxation on those who could best afford to pay it by reason of increased incomes due to the war. An examination of the income-tax returns of taxicab companies will, we believe, demonstrate that there has been no increased income due to the war. In the case of the taxi service company, the gross receipts of the company since the beginning of the war have decreased continuously from month to month in the face of rising costs of labor and material of every kind. In no year since its existence has the company's net earnings been equal to 5 per cent of its gross receipts, and in the past five years have averaged only 4 per cent.

We assume that it was certainly not the intention to drive taxicabs out of business, as it is beyond argument that the services performed by such companies in the transportation of persons is a highly useful and important business. In these times a large part of the business of this company consists in the transportation of business men from place to place within the city and to and from railroad stations, thereby saving valuable time and facilitating the transaction of business within the city of Boston. The amount of riding for pleasure and recreation has shown a very sharp decline since the beginning of the war.

One of the principal items of expense in the taxicab business is gasoline. Section 902 of the bill imposes a tax of 2 cents a gallon on gasoline. Even on the basis of the present reduced consumption of gasoline, the additional expense entailed by such a tax would amount, in the case of the taxi service company, to between 1 per cent and 1½ per cent of its gross receipts. Another heavy item of expense in the case of taxicab companies is tires, parts, and accessories, on which section 900 places a tax of 10 per cent. In addition, section 1006 of the bill imposes a special annual excise tax on automobiles, varying from \$10 to \$50. As this company operates over 200 automobiles, this tax alone would probably amount to about 1 per cent of the gross receipts.

It is apparent that, with these special taxes on gasoline, tires, parts, and accessories, and the annual excise tax on the use of automobiles, persons operating taxicabs generally, in this country, will in the face of the continued decline of business, have a struggle for existence during the continuation of the war. Therefore, to single them out from all businesses in the country as subjects of additional special taxation, on the basis of their total gross income, would not only be a discrimination contrary to the basic principle of the pro-

posed legislation, but would almost certainly result in the crippling of a service that has come to perform an important and necessary function in the transaction of the country's business.

As experience has shown that it is extremely difficult, if not impossible, to obtain an increase of rates for taxicabs, it is suggested either that paragraph 12 of section 1001 of the bill be amended, so as to except from the operation of the tax companies operating passenger automobiles for hire, whose rates are subject to regulation, or else to place the taxicab companies on the same basis as all other companies transporting passengers for hire by providing that the tax shall be paid by the person paying for the service rendered. If the law provided that, in addition to the legal rate of fare, there should be a tax of 5 cents on each ride where the fare was \$1 or less, to be paid by the passenger, and an additional 5 cents for each additional dollar or fraction thereof, the amount of revenue raised would be far greater than under the present proposed law.

Senator THOMAS (in the chair). The committee will now hear from Mr. Francis B. James. Mr. James, how much time do you want?

STATEMENT OF MR. FRANCIS B. JAMES, REPRESENTING THE CAMPBELLS CREEK COAL CO.

Mr. JAMES. Not to exceed 10 minutes. I have prepared an amendment which I am asking for, and a memorandum in support of it, which I would like to have circulated before my presentation.

Section 234a of the bill on page 36 provides, "That in computing net income there shall be allowed as deductions," etc., and among others, deduction number eight (8), which appears at page 37 which provides [reading]:

(8) In the case of buildings, machinery, equipment, or other facilities, constructed, erected, installed, or acquired, on or after April six, nineteen hundred seventeen, for the production of articles contributing to the prosecution of the present war, there may be allowed a reasonable deduction for the amortization of such part of the cost of such facilities as has been borne by the taxpayer, but not again including amounts otherwise allowed under this title for depreciation, exhaustion, or wear, and tear.

We are asking permission to insert after the word "production," in line 22 on page 37, the words "or transportation by inland waterways." A great deal of the coal is moved to the market in the West down the inland waterways of the country. The particular company I speak for has a river tipple at Dana on the Kanawha River. The coal is carried to Point Pleasant on the Ohio, with four barges making the trip back and forth until about ten barges are assembled. These barges are then towed by a tow boat, with all the dangers of inland navigation. Last winter 42 of our barges, representing a book value of \$47,000, were carried away by the ice. It has cost us \$167,000 to replace those barges. Instrumentalities for the production of coal may be amortized. The coal is useless unless it is transported by these inland waterways.

We believe that the same principle might be applied to these barges and towboats which are used for the transportation and marketing of this coal down the Kanawha and the Ohio Rivers. We are asking, therefore, that this be extended not only to the vehicles, as is here spoken of, and instrumentalities for the production and transportation of coal, which is conceded to be an article contributing to the prosecution of the present war as much as any commodity known, but it should be extended likewise to these instrumentalities

for the transportation, making possible the use of this coal. And this is particularly true now with the necessity for relieving the use of the railroads by encouraging as much as possible those people who have put their money into barges or boats on these inland waterways.

Senator McCUMBER. Are you not allowed to charge this loss against profits?

Mr. JAMES. We are not now; no, sir.

Senator THOMAS. The amendment proposed to the bill does not limit its operation to coal companies.

Mr. JAMES. No, it would not be limited to coal companies. As a matter of fact, the package freight has practically disappeared from transportation on inland waterways. Transportation now is largely confined to the heavy commodities such as coal and some others; also forest products; but largely on the inland waterways of the West it is confined, in the territory that I am familiar with, to the transportation of coal in large quantities. I will not say that there is no package freight, but there is very little package freight.

Senator PENROSE. In the East there is lumber and other bulky propositions.

Mr. JAMES. Yes, and I do not see why that should not apply to those large commodities which are useful in the prosecution of the war.

Senator PENROSE. I do not, either.

Senator THOMAS. I do not.

Mr. JAMES. The reason I did not want to go on with regard to other things is that my own experience is with coal and lumber upon these inland waterways in that section.

Senator PENROSE. I think it ought to apply to all of them.

Senator GERRY. Most of our coal in New England comes by barge.

Mr. JAMES. Yes.

Senator THOMAS. But not on inland waterways.

Senator GERRY. Hardly.

Mr. JAMES. The loss does not exist to the same extent in the coast-wise trade as it does in the inland waterways. They freeze up every winter. For example, take this particular company; one-third of its investment in barges and towboats was swept away last winter.

Senator LODGE. They do not meet submarines or heavy seas on the inland waterways.

Mr. JAMES. Yes, of course they have their danger from submarines now.

Senator LODGE. And they have heavy losses from bad weather.

Senator GERRY. Yes; a good many were lost this year.

Senator SMOOT. Yes. There were heavy losses in the Potomac, too, because there was an ice gorge formed there.

Senator GERRY. Yes. It was the same all up the coast.

Senator SMOOT. The loss was heavy at Providence, R. I., with which you are familiar.

Senator GERRY. Yes. At the present time coal goes to Virginia ports, and is taken up to Providence by barge.

Mr. JAMES. I am particularly familiar with that situation in the West as to inland waterways, and I think these words should not be

left out, but should be inserted so that it will apply to the transportation of these bulky things useful in the prosecution of the war.

(The memorandum submitted by Mr. James is here printed in full, as follows:)

PROPOSED AMENDMENT.

In line 22, page 37, paragraph (8) of section 234a of House bill 12863, entitled "A bill to provide revenue, and for other purposes," insert the words "or transportation by inland waterways" after the word "production."

MEMORANDUM.

Owing to the severe weather of the past winter there was a great destruction of barges and towboats on the inland waterways transporting coal and it became necessary to replace same at very great cost.

This will be illustrated by the case of the Campbells Creek Coal Co., which has a river tipple at Dana, W. Va., on the Kanawha River. Coal is transported from Dana down the Kanawha River to the Ohio River and thence down the Ohio River for distribution to towns and cities located thereon. Some 42 barges were destroyed, having a book value of approximately \$47,000. To replace same will cost at war-time prices approximately \$160,500. When the war is over these barges will have an approximate peace time book value of \$47,000, or about \$100,000 less than the war-time replacement cost. The new revenue bill allows amortization only for buildings, machinery, equipment, or other facilities for the production of coal, but does not cover the matter of amortization for the equipment and facilities for the transportation of such coal on inland waterways.

Production of such coal is useless unless it can be transported. The Campbells Creek Coal and other companies are performing a public service in the transportation of such coal by the inland waterways, thus greatly relieving the railroads. Amortization ought, therefore, to be equally applicable to equipment and facilities for the transportation of such coal on the inland waterways as to the equipment and facilities for the production of coal.

The CHAIRMAN. The committee will now adjourn until to-morrow morning at 10.30 o'clock.

(Thereupon at 5.15 o'clock p. m. the committee adjourned until Friday, September 13, 1918, at 10.30 o'clock a. m.)

TO PROVIDE REVENUE FOR WAR PURPOSES.

FRIDAY, SEPTEMBER 13, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met pursuant to adjournment at 10.30 o'clock a. m., in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present: Senators Simmons (chairman), Thomas, Robinson, Gore, Jones, Gerry, Nugent, Penrose, McCumber, Smoot, Townsend, and Dillingham.

The committee resumed the consideration of the bill (H. R. 12863) to provide revenue, and for other purposes.

The CHAIRMAN. Mr. Goldberg, I notice that Mr. Neurat is to talk upon the same subject you will speak of. Do you both want to be orally heard?

Mr. GOLDBERG. We prefer that. I will have only a very few words to say.

DISTILLED SPIRITS.

STATEMENT OF MR. MARK GOLDBERG, OF NEW YORK.

The CHAIRMAN. Is it the same subject?

Mr. GOLDBERG. It is the same subject.

The CHAIRMAN. Are you going over the same ground?

Mr. GOLDBERG. I was not going into the merits of the items Mr. Neurat will speak of. I was simply going to give my ideas.

The CHAIRMAN. How much time do you want?

Mr. GOLDBERG. I would not take 5 minutes, and probably Mr. Neurat would not take 10.

Fortunately or unfortunately, I have been a member of the New York State Legislature for about 12 consecutive years and expect to go back for my thirteenth year. I have had the honor of being chairman of the committee on taxation and retrenchment in the assembly and also the judiciary committee during the Democratic years, and I realize the absolute necessity of raising revenue under these conditions. I represent the Family Wine and Liquor Dealers' Protective Association of the State of New York. We have about a thousand men in that association. We are what they so call in the State of New York the holders of license No. 2, who can only do business for consumption off the premises. We are not the saloon keeper, but we are the family store, and everything that you buy on our premises you must take home with you and consume home.

Senator PENROSE. What is the smallest amount you can sell under that license?

Mr. GOLDBERG. The largest amount is 5 gallons.

Senator PENROSE. There is no minimum amount?

Mr. GOLDBERG. There is no minimum, but whatever we sell must be consumed off the premises. Under this Title No. 6 the burden of taxation is going to fall the heaviest on us. We are willing, and have been willing, and have, I believe, shared our proportionate burden of the taxation under the old revenue bill, and I think that the record will show that we stood up and did our duty.

We are willing to do the same if permitted to remain in business. But from my legislative experience it seems to me that the tax that you impose now on beverages will be confiscatory. It will mean the driving of these people out of business. I say that frankly, because I probably realize the situation in the States better than even you gentlemen here, living in the States and knowing the conditions of the business.

By way of illustration, under the State law the holder of a No. 2 certificate had to file with the excise commissioner a notice on or before the 15th of August to show his intention to do business, and if he failed to do that he was deprived of his license, beginning with October 1. There were probably 300 men who failed to file this year their intention to do business.

Senator PENROSE. How much do they pay for that license?

Mr. GOLDBERG. \$1,200.

Senator PENROSE. A year?

Mr. GOLDBERG. A year—\$100 a month. They failed to file that notice as provided in the excise law of the State, and the department said they could not go back of the law, and they would not issue any license to them. Realizing that the number who failed to file certificates would mean probably a loss of \$300,000 to the State of New York, the excise department, notwithstanding this law that they maintained was a condition precedent to the issuing of a license, have recalled that notice and now state that they will issue licenses to these people because they can anticipate this condition, but the depriving of 200 people of doing business in the State will deprive the State government of over \$300,000.

October 1 is the day on which these licenses are issued. There are a number of people just waiting to see what you gentlemen are going to do. The tax you have levied now is a confiscatory tax. They can not pay it.

The CHAIRMAN. What specific tax do you refer to? I know the general tax to which you are addressing yourself, but what is the specific tax?

Mr. GOLDBERG. The tax on whisky, which will be \$8.

The CHAIRMAN. You say that is confiscatory?

Mr. GOLDBERG. I say it is confiscatory, as also the tax on the light wines. It means that if they find you gentlemen come to the conclusion you are going to carry into effect the provisions, they will not take out their licenses beginning with the 1st of October. It would be better for them to simply turn over the key to the Government and say, "Here is our merchandise," than apply for a new license under the State law, pay the Government tax that you anticipate levying, and also pay the State tax. The State tax is

very heavy. They levy a tax under the State excise law of a certain percentage on your gross receipts.

Senator PENROSE. What is that percentage?

Mr. GOLDBERG. It varies. A No. 2 license, if the licensee does between \$12,000 and \$15,000 worth of business, has to pay 1 per cent on his gross receipts, and if he does over \$15,000 to \$20,000, he has to pay 2½ per cent. In addition to that, he had to pay the tax you have levied under your old revenue bill, and then this new tax.

Senator THOMAS. Are you required to pay a city license also?

Mr. GOLDBERG. No; you do not have to pay a city license. If, in addition to that, you sell quantities of over 5 gallons, you have to take out a malt license, and if you sell whisky over 5 gallons, you have got to take out a Government license.

In addition to that, this extra tax will practically mean the turning of the key. Especially is this so in view of the prohibition that is in the air.

Senator NUGENT. You have been aware of the fact that this is in the air for some time, have you not?

Mr. GOLDBERG. It has been in the air, and I think it might be advisable, although coming very humbly from me, to keep it in the air until the war is over. I do not think this is the time for prohibition. If I could, without wanting to in any way—

Senator ROBINSON. May I suggest that you confine yourself to the topic under discussion?

The CHAIRMAN. Yes; I think that would be the better plan. What we want to hear you about is the specific matter you are interested in and that you want relief against. This is not any place for making speeches.

Mr. GOLDBERG. No; I do not wish to make any speech, except that the Senator spoke about it being in the air.

Senator SMOOT. What suggestion have you to offer as to changing the bill?

Mr. GOLDBERG. I ask you gentlemen to take that matter seriously into consideration, because October 1 is the beginning of the fiscal year in the State of New York. If the tax is levied as proposed, in our opinion it will be confiscatory and these people will have to go out of business.

Senator ROBINSON. You have no specific suggestion to make?

Mr. GOLDBERG. No; I am going to leave it to Mr. Neurat.

Senator PENROSE. Do you think the trade could stand any increase of tax?

Mr. GOLDBERG. Yes, sir; I do. I think they are willing to stand a fair increase in tax.

Senator PENROSE. What would you call a fair increase?

Mr. GOLDBERG. I was going to leave that for Mr. Neurat.

Senator PENROSE. You have some idea, have you not? You have talked with him?

Mr. GOLDBERG. I would prefer for you to get his ideas of that. We are willing to pay a fair increase so that we can continue and remain in business as long as the Government thinks we ought to.

The CHAIRMAN. It does not help us much to say a tax is confiscatory unless you are going to give us some evidence to sustain your allegation.

Mr. GOLDBERG. I will submit a brief.

The CHAIRMAN. I think, from what this gentleman says, he has pretty nearly made out a case.

Senator PENROSE. I do not see how they can dispose of these articles under the State and national taxes.

The CHAIRMAN. We can now hear Mr. Neurat. You may proceed, Mr. Neurat.

STATEMENT OF MR. ADOLPH NEURAT, OF NEW YORK CITY.

Mr. NEURAT. Mr. Chairman, Mr. Goldberg has covered practically the entire question, as far as the taxes on the whiskies being confiscatory is concerned. But I want to dwell first on the fact that you made a provision of taxing the stock on the floor with the additional taxes of \$4.80 per proof gallon. But you failed to make provision for a return to those men who may be barred from doing business with the public on account of the various laws which have been passed giving the President of the United States the power to declare war zones, and giving the power to the States to declare prohibition by July 1.

There are in the State of New York several millions of gallons of liquor held on store tax paid now. With this confiscatory tax of \$8 per gallon it will be absolutely impossible to dispose of these goods during the period of time allowed. I and my colleagues who are engaged in the business will be compelled by law to lay out this money. For instance, I want to state myself that I hold probably 5,000 gallons of liquor in my establishment. Under the present statute I will be called upon to lay out \$22,000 cash money to the Government, and I am situated in a section that may be declared a war zone at any time. What will become of my money or my colleague's money, who has invested every blessed dollar that he has earned all during his lifetime? I appeal to you that this is not American to take a man's money without giving him a chance to sell his merchandise.

We are willing to stand by the Government. We have stood by the Government prior to this and paid our \$3.20, and we have not disposed of the stock that we have paid on our first revenue bill of October 3 of last year. Now, here you come along and you say, "You have to give us \$4.40 more, and we are giving you restrictions as to the disposal of your merchandise."

Senator SMOOT. Did you not take your 5,000 gallons out before the increase of tax was imposed?

Mr. NEURAT. Last year!

Senator SMOOT. Yes; before the revenue act of 1917?

Mr. NEURAT. Yes. I paid last year eighteen thousand and several hundred of dollars to the Government. And as the tax was levied the merchandise was increased to such a volume of price, the consumption of liquor lessened, and we have this merchandise on hand.

Senator SMOOT. But you have made more money on it, have you not, than you ever made in your life before?

Senator PENROSE. He paid the full tax.

Mr. NEURAT. I do not believe we made as much, Senator.

Senator SMOOT. You know so; I do not. I know this, that there have been many, many millionaires made from the increased price of liquors.

Mr. NEURAT. I want to say this, that the millionaires to whom the Senator is alluding are the distillers and the gamblers, who have bought up and cornered the whisky market, who held the papers in bond, and then went out and sold it at a prohibitive price. Goods that were manufactured at 25 cents per gallon were selling at \$3 per gallon in bond, and it was the large men who were made the millionaires, but the poor retailer man has not made a button.

Senator SMOOT. When did you take your liquor out of bond?

Mr. NEURAT. I have taken my liquor out of bond—

Senator SMOOT. What time did you take it out? What was the date?

Mr. NEURAT. I take liquor all the time out of bond. But before last October, you mean?

Senator SMOOT. Yes. How much did you take out before October of last year and had you on hand?

Mr. NEURAT. I had over 9,000 gallons on hand.

Senator SMOOT. In other words, you have made on the 4,000 gallons you have sold between that time and now whatever advance there has been upon that liquor, and you got it at the old rate imposed, did you not?

Mr. NEURAT. The profits that I have made, or that could be made, on the 4,000 gallons of liquor have not paid the expenditures of the whole year's business. You misunderstand the question of the expenses of carrying on the retail liquor business. Everything costs money.

Senator SMOOT. Yes; I know that.

Mr. NEURAT. And the profits are less. We used to make more money working on a basis when the tax was \$1.10 than we are now when the tax is \$3.35.

Senator SMOOT. But if you got your liquor at \$1.10 and work on a basis of \$3.20, you ought to be that much better off?

Mr. NEURAT. It may be, in your mind.

Senator GORE. He takes it in, but he has paid it out already.

Mr. NEURAT. That is all I would bring before your attention. We are willing to suggest to the committee, as Senator Penrose said, that we are willing to be honest, we are willing to be honorable, but \$8 tax is absolutely prohibitive. It would make a gallon of liquor cost a man to purchase in the trade from \$14 to \$16 a gallon. How could he sell it? It would be not only prohibitive, it would be a luxury. It would be worse than wearing jewelry, etc. If this committee would pass a tax, we will say, of from \$3.20 to \$5 a gallon, we would strive hard to make this go, and help the carrying on of our burden of the war. But if you make it \$8 a gallon, I will assure you that this tax is not going to be a producer. It is going to be a reducer of taxes instead of being a producer of taxes.

Senator THOMAS. Your position virtually is that as a citizen you ought not to be taxed very heavily by one statute and put out of business by another?

Mr. NEURAT. That is right.

Senator THOMAS. I think you are right.

The CHAIRMAN. How many gallons of liquor do you sell a year in your establishment?

Mr. NEURAT. Prior to the war we were selling, I judge, about 400 gallons of liquor a month. Since the first taxes were put on we have not disposed of 100 gallons a month.

Senator PENROSE. You operate under license No. 2, which has been referred to?

Mr. NEURAT. Yes, sir. I sell to the families; not consumed on the premises.

The CHAIRMAN. You say you are selling now but 100 gallons a month?

Mr. NEURAT. Yes.

Senator SMOOT. Then you will not have to pay any tax at all for two years.

Mr. NEURAT. Why not?

Senator SMOOT. Because you have liquor enough on hand.

Mr. NEURAT. You are making your provision for a floor tax. I will have to pay that tax just the same.

The CHAIRMAN. You say you have on hand now 5,000 gallons. When did you buy that?

Mr. NEURAT. I bought some during the year, during the time since last October, and I have always carried whisky in bond.

The CHAIRMAN. During what year did you buy that large amount of liquor?

Mr. NEURAT. I bought quite considerable after the war tax was placed on it, because the market is rising.

The CHAIRMAN. After the first war tax?

Mr. NEURAT. After the first war tax.

Senator SMOOT. You could not have bought very much, because you had 9,000 gallons on hand when the law went into effect, and you have 5,000 now. That is 4,000 difference, and if you sold 400 gallons a month, that is 4,800.

Mr. NEURAT. I want to state that I always, even now, have several hundred barrels of whisky in bond which I have not on the floor. At that time, before the last tax, I used to do a big business.

The CHAIRMAN. When did your sales fall down to 100 gallons a month?

Mr. NEURAT. The sales fell down right after last Christmas.

The CHAIRMAN. So that this year you have been selling only 100 gallons a month?

Mr. NEURAT. That is about all.

The CHAIRMAN. Have you bought any whisky this year?

Mr. NEURAT. I have bought some in bond, but I have not bought any on the floor.

The CHAIRMAN. When you had a large amount on the floor of your establishment, and your sales fell down to 100 gallons a month, why did you go and buy some more whisky?

Mr. NEURAT. Because we all trade in papers, the same as Wall Street.

The CHAIRMAN. You did what?

Mr. NEURAT. We have traded in papers, in bond, buying whisky in bond and selling it to-morrow in bond, without handling it, to the trade.

The CHAIRMAN. You were speculating?

Mr. NEURAT. Speculating; yes.

The CHAIRMAN. You said a little while ago that you were in danger of having your liquor confiscated peremptorily by reason of being possibly in some war zone.

Mr. NEURAT. Yes, sir.

The CHAIRMAN. If you are in a war zone, or if the place you are now in is declared to be a war zone, why can you not sell that whisky in New York to some one who is not in the war zone?

Mr. NEURAT. Under this present bill there is no one now buying any whisky. They are all trying to sell, and I think if you go around from storekeeper to storekeeper you will find they are all ready to give up, as long as they can get 100 cents on the dollar for their merchandise. There is no one ready to buy.

Senator THOMAS. You know the new prohibition law permits you to export it to other countries so that they can drink.

Mr. NEURAT. I know that.

Senator ROBINSON. What do you think would be a fair tax in lieu of the tax provided in this bill?

Mr. NEURAT. I think \$5 would be fair, and it may work out. But I doubt very much that the present tax will work out.

Senator GORE. Do you think the saloon could stand a higher tax than you could stand? Is there such a difference between the family business and consumption in saloons as would enable them to pay a higher tax than you could pay?

Mr. NEURAT. I do not think so, Senator.

Senator PENROSE. Do you think the Government would get more money out of a \$5 tax than out of an \$8 tax?

Mr. NEURAT. Positively.

Senator PENROSE. According to your view the Government would not get any revenue out of an \$8 tax?

Mr. NEURAT. I do not believe the Government will get much tax. You know these gentlemen here must not forget that although the Internal Revenue department may show that they have collected so many millions of dollars in revenue last year for whiskys, etc., most of which came from floor tax. I believe the Government collected last year close to \$135,000,000 just for floor tax, this \$135,000,000 which they claim in their depositories to-day will not go in now, because there is an awful amount of that whisky still laying out, and whiskys have not been taxpaying this year as fast as they were last year, which shows that the consumption is much less.

The CHAIRMAN. You are a wholesaler?

Mr. NEURAT. Yes, sir.

The CHAIRMAN. What do you sell your liquors at?

Mr. NEURAT. A gallon?

The CHAIRMAN. Yes.

Mr. NEURAT. Liquor sells to-day from \$8 to \$12 a gallon. It depends upon the quality and age.

The CHAIRMAN. Leaving out the tax, what do you pay for liquor in bond, if you buy it in bond? I mean, what price do you pay in excess of the tax in effect at the time of the purchase?

Mr. NEURAT. Do you mean what the naked whisky would cost in bond?

The CHAIRMAN. The naked whisky.

Mr. NEURAT. About \$3.25 a gallon, to-day.

The CHAIRMAN. Whisky in bond costs \$8 to \$8.25 a gallon, nothing but the whisky?

Mr. NEURAT. Nothing but the whisky. That does not include any taxes, any railroad rates, and all the expenses attached to it.

The CHAIRMAN. Is that about the average price you have to pay?

Mr. NEURAT. That is the average price.

Senator PENROSE. What does it cost the distiller to make?

Mr. NEURAT. That is just what this Senator here has said, that we made so many millions. It cost the distiller about 60 cents to make, and he sold it to us for \$3 to \$3.50.

Senator THOMAS. When you say you sell whisky for \$3 do you mean the distilled or the rectified?

Mr. NEURAT. No; that means the straight whisky in bond, without any tax or anything else.

Senator THOMAS. What does the rectified whisky sell for?

Mr. NEURAT. Retail, from \$8 to \$12 a gallon.

Senator THOMAS. That is higher than the other.

Mr. NEURAT. We have to put on \$3.35 tax, freight, etc.

Senator JONES. What was whisky selling for in bond, without any taxes, before the war?

Mr. NEURAT. About 65 or 75 cents a gallon.

Senator JONES. What raised the price from 65 to 75 cents a gallon to \$3 a gallon?

Mr. NEURAT. The distillers raised the price. When they were prevented making it last September they said: "We have only so much to sell, and we are going to make all we can out of it."

Senator GORE. If the distillers were to take 65 cents now, or even a dollar, and added \$8, that would make \$9, and that is \$3 less than you are selling it for. So if the distillers would return to the old price it could still be handled under an \$8 tax, could it not?

Mr. NEURAT. No; because you forget that the retailer has to pay about 33½ per cent gross expenses on his sales. He could not make a living out of that.

The CHAIRMAN. When did that whisky go up to \$3.50. You said it used to sell for sixty-odd cents.

Mr. NEURAT. Right after distillation had been stopped—after last September the 8th.

The CHAIRMAN. I understood you to tell Senator Smoot a little while ago that you bought this 9,000 gallons that you had in stock before last October.

Mr. NEURAT. Oh, yes. I bought the biggest part of it.

The CHAIRMAN. Then you got this enormous quantity you have in stock at the rate of 60 cents, less the taxes?

Mr. NEURAT. Oh, no. There was no 60-cent whisky when I started to buy.

The CHAIRMAN. I understood you to say just now that up to last September, when they stopped distillation, you could buy this liquor free of tax, or without a tax, in bond for about 60 cents.

Mr. NEURAT. So you could.

The CHAIRMAN. But since that time it has been selling at about \$3.50.

Mr. NEURAT. Right.

The CHAIRMAN. I understood you to say that you bought this 9,000 gallons before last October.

Mr. NEURAT. Yes.

The CHAIRMAN. So you must have gotten this 9,000 gallons at 60 cents, if you did not pay more than you say liquor was selling for at that time. You have a big profit if that is so.

Mr. NEURAT. No, Senator, I do not want you to misunderstand. If the Government had not changed any other taxes from \$3.20 up to \$8, or up to \$5, I might have made my profit in the course of the long run. But if the taxes now are going to be changed again there is no profit; there can not be any profit. I have a stock which I am unable to dispose of. In other words, I have \$9,000 or \$12,000 worth of stock, which cost me, naked, without the revenue, that, and if I can not sell it what good is the profit?

Senator PENROSE. What you mean to say is that if you have made profits up to date they will be wiped out by your being stuck with the stock you have?

Mr. NEURAT. Positively.

The CHAIRMAN. That is an apprehension. You have from now until next July to dispose of this liquor. You say you are really afraid you can not dispose of it if we increase this tax to \$8?

Mr. NEURAT. Yes.

The CHAIRMAN. And apply that to the floor stock.

Senator JONES. If you were to offer your certificates for sale at the price which you paid for them, have you any doubt that you could sell them at that price?

Mr. NEURAT. No, sir.

Senator JONES. Are you willing to take the price you paid for them?

Mr. NEURAT. Yes, sir.

Senator JONES. How much was it?

Mr. NEURAT. I think my average whisky stands me about \$1.50 to \$1.75 per gallon, and I will take it now and retire. You can not sell to-day any certificates.

Senator GORE. Why is it that it is so high and yet you can not sell it? Why do they not put down the price and see if there would not be buyers at a lower price?

Mr. NEURAT. Because everybody paid the price for it, and they can not go out of business without making that amount.

Senator GERRY. Has the distiller sold a large quantity of his whisky that he has in bond?

Mr. NEURAT. I do not think the distiller to-day owns one barrel in bond. The distiller unloaded to men like me and my colleagues all over the country. They got rid of theirs, and they do not worry whether you pass prohibition or whether you pass a \$10 tax on it. Their worries are over.

Senator PENROSE. Do you mean to say that the stock of whisky in the country is held by the retailer and the wholesaler?

Mr. NEURAT. Yes, sir; positively.

Senator PENROSE. And the distiller has disposed of all his holdings?

Mr. NEURAT. The distiller has disposed of his holdings.

Senator SMOOT. Not all of them. We had a distiller here the other day.

Mr. NEURAT. I want to say that they disposed of 90 per cent of their holdings. I want to say to Senator Penrose that to-day the millionaires who were made—and I agree with Senator Smoot that they made an awful lot of money—made their money by bleeding the retail liquor man and trying to boost him with statements like this, "We have prohibition this" and "We have prohibition that."

Mr. Distiller does not come before you and say, "Do not give the retailer the tax." He wants the poor retailer to come up to-day and plead with you. If the distiller was to be taxed, he would be here, but he is not here to represent himself. He has nothing to represent. He has no hearing to give you. He has unloaded his holdings to me and my friends and my colleagues.

Senator SMOOT. For speculative purposes?

Mr. NEURAT. And therefore he does not care whether we are put out of business to-morrow or not.

Senator JONES. Is it the retailer or the speculator who is complaining of this tax?

Mr. NEURAT. No, sir; it is only the retailer. There is no speculator. The retailer holds the stock whether on his floor or in bond, and if he can not get rid of it there is no use talking.

Senator JONES. Did you not admit you were holding yours for speculation?

Mr. NEURAT. At that time, when the manufacture of whisky was stopped, I bought on speculation. And not only I, but I want to say to you that Senators—probably I do not know whether Senators did, but I know legislators and doctors and everybody else—bought whisky on a speculative basis at that time, thinking there was going to be a gold mine in it.

Senator SMOOT. And the distillers sold.

PASSENGER AUTOMOBILES.

The CHAIRMAN. The next gentleman desiring to be heard is Mr. John J. Fitzgerald.

STATEMENT OF MR. JOHN J. FITZGERALD, OF NEW YORK, N. Y.

Mr. FITZGERALD. Mr. Chairman and Senators, I appear to request that paragraph 12 of section 1001, title 10, fixing a tax of 5 per cent upon the gross receipts of companies operating three or more automobiles, be eliminated from the bill.

In the first place, it is difficult to understand why any business should be selected for this tax on its gross receipts; and if it should be deemed necessary to select a particular business for such a tax, it is inexplicable that in so doing the great bulk of the business should be eliminated from the tax and a tax levied only upon the responsible portion of the business and that portion of the business which has done so much to make the taxicab business safe and respectable. The Black and White Town Taxis (Inc.) is the largest operating taxicab company in the city of New York. It operates 425 taxicabs.

Senator LODGE. What is the total number of taxicabs in New York?

Mr. FITZGERALD. The total number of taxicabs in New York City is 3,488; 755 are operated by the companies, and the balance, 2,733, are operated by the so-called "bucker," as he is known in New York, or "skinner" in other sections of the country.

Senator THOMAS. How many companies are there that this tax will affect?

Mr. FITZGERALD. There are four large operating companies.

Senator THOMAS. How many small?

Mr. FITZGERALD. And then there are some smaller ones. But the great bulk of the other cabs are operated by the individuals. A great many of the individual operators buy their cabs on the installment plan, the same as they bought the old hack, paying \$100 or \$200 down and giving back a chattel mortgage on the cab. In case of accident to a passenger or injury to a pedestrian or accident by collision due to the gross negligence even of the operator of the cab, when the person injured comes to secure his redress he finds an absolutely irresponsible person financially against whom to collect. The Black and White Town Taxis (Inc.) is the largest operator. It operates 425 cabs. It has two classes of service, one they refer to as their *de luxe* service, in which they use 174 cabs. That is practically a charge service. They serve all the clubs in the city of New York, and the payments are not cash payments, but are charge accounts. It requires the maintenance of numbers of starters at all the places where cabs are supplied. It requires the maintenance of a considerable force for their accounting system.

The rates charged for that service, fixed by the ordinances of the city of New York, are 30 cents for the first quarter of a mile and 10 cents for each additional quarter of a mile for one or two passengers, and for three or more passengers 30 cents for the first third of a mile and 10 cents for the additional distances.

Then they operate what is known as the popular service, the service which is doing so much to popularize the use of the taxicab at reasonable compensation. They operate 251 cabs, and the charge made, regardless of the number of passengers, is 10 cents for the first third of a mile and 10 cents for each additional one-sixth mile. Five persons can travel from the Knickerbocker Hotel to the Grand Union Depot in New York for 10 cents in a Black and White taxicab.

Their estimated receipts for this year are \$3,000,000. For purposes of taxation their invested capital is about a trifle over \$600,000. Arthur Young & Co. chartered public accountants, who audit their books, were requested to make an estimate of the effect of the taxes in the proposed bill upon their business. Estimating net profits, without paying any Federal taxes whatever, of \$120,000, under the proposed bill they have these additional charges: Two cents a gallon on gasoline, using 1,000,000 gallons of gas, will add \$20,000 to the amount of their taxes. Ten cents extra on the purchase of an estimated consumption of \$150,000 of tires and other accessories adds \$15,000; \$10 on each of the 425 automobiles operating under the tax on automobiles, their automobiles coming in the lower class, being cars of about 22 horsepower, \$4,250. The new taxes, outside of this tax on the gross receipts, aggregate \$39,250. Estimating the net profits for 1918, after paying the new taxes other than income and excess-profits' taxes, their net profit would be \$80,750.

The CHAIRMAN. Let me ask you a question right there: In the last estimate, do they take into consideration the probable increase in their prices that they will make?

Mr. FITZGERALD. Their prices are regulated by ordinance, and the committee will appreciate the impossibility of any increase of the rates allowed by ordinance when a common council in a great municipality will be confronted with the proposition that the rates should be raised in order to help out the operators of 755 cars, when the 2,700 and odd cars need not be affected by this tax at all.

The CHAIRMAN. Then you are assuming that the municipal authorities of the city of New York will not permit, under the ordinance, an increase in the rates of these automobiles, notwithstanding the tax imposed by the Federal Government?

Mr. FITZGERALD. We assume that for this reason: In the first place, after a great deal of controversy the rates have been fixed. In the second place, to increase the rates for taxicab hire, in order to accommodate those who come within this law, the operators of 2,700 and odd cabs out of the 3,500 cabs in that city alone will be given a gratuity by the Government, because they will charge the tax and put it in their pockets.

The CHAIRMAN. Could not your common council fix one rate for an automobile that has to pay a Federal tax and a different rate for a cab that does not have to pay it?

Mr. FITZGERALD. It is absolutely impracticable to levy such a tax as this, and to collect it, unless from the responsible companies. No one has any record or knowledge of what the man who operates his own cab collects. He keeps no books, he has no records, he makes no accounting; nobody can tell how much business he does. So that unless it is a reputable company, with an organized system and a bookkeeping system, no one could tell what was made.

The CHAIRMAN. All I wish to do, Mr. Fitzgerald, is to inject, in connection with your estimate there, the fact that that was based upon the hypothesis that there would be no increase in rates, either made arbitrarily by the owners of these automobiles or permitted by the common council of the city of New York.

Mr. FITZGERALD. That is the basis of that argument; but under the present law the net results to the company would be about \$98,000, under the proposed taxes \$58,000, out of a business of \$3,000,000. If a 5 per cent tax on gross receipts was imposed, instead of being a net return to the company of \$58,000 there is a deficit, without paying a single dollar in taxation to the Federal Government. That will run in the neighborhood of \$90,000, and it means, with a proposed tax such as that, that that company must stop operation.

That situation in the city of New York is identical with the situation in all of the great cities of the United States. The representatives of the leading taxicab operators from Boston, Baltimore, New York, Washington, and Philadelphia were in conference last night. There are in the city to-day the representatives of the operating cabs in Chicago. They do not wish to be understood as objecting to any class of taxes that are believed essential at this time in order to raise the very extraordinary revenues required. All they ask is that they be put upon an equality with everybody in their business. All they ask is that everybody with whom they must compete be placed upon the same basis.

In addition to the occupation tax, the tax upon the automobile based upon the horsepower, the tax upon gasoline, and the tax upon tires and accessories, if it then be believed essential, in order to produce additional revenue, they are willing to have an additional tax put upon them. They make a suggestion that if they are to be singled out, that a tax can be levied upon automobiles used for the transportation of passengers for hire that they believe will produce a revenue far in excess of anything contemplated in this provision, and their suggestion is that if it be deemed necessary to single out

this business for some special tax instead of a tax upon the gross receipts, that, in addition to the tax they must pay upon their automobiles based upon horsepower, a flat rate of \$20 be put upon each car used for the transportation of passengers for hire. Outside of the large cities or the relatively large cities there are hundreds of thousands of automobiles used for this purpose. They are operated by the owner of the car. As a rule, he will not own more than one or perhaps two cars. He escapes under this proposed tax. It is estimated conservatively that 500,000 automobiles are used in the United States for taxicab purposes, and if the committee believe it is essential or desirable to single this particular business out for a special tax, in addition to all the other taxes imposed upon them, \$20 a year per car would not be sufficiently burdensome to affect any individual operating a single car and yet would produce a revenue of \$10,000,000.

Senator ROBINSON. That would also reach the "skinner" and would prevent any possibility of their evading it.

Mr. FITZGERALD. And the "bucker." That would be an additional tax to this particular company of \$9,000 a year, that \$20. These men do not believe there is any special reason for a peculiar tax upon their industry. This is one of those rare occurrences in a revenue bill that comes from the House where an imperfection has slipped into an otherwise perfect bill.

Senator THOMAS. Your estimate of \$20 per vehicle would give very nearly \$70,000 from the city of New York. You say there are 3,488 taxis in New York?

Mr. FITZGERALD. Yes, sir.

Senator THOMAS. At \$20 per vehicle, that would be \$69,760 from the city of New York, and distributed equitably among all those in the business.

Mr. FITZGERALD. Yes, sir.

Senator ROBINSON. That would raise between eight and ten million dollars, in all probability, levied throughout the country?

Mr. FITZGERALD. They estimate there are about half a million cars throughout the country. As a matter of fact, it is not believed that there is any reason for it. There is a belief, due to our own peculiar experiences at times in the use of the taxicab, that the taxicab business is an inordinately prosperous business. The history of taxicab companies in the great cities is that the great percentage of them go into bankruptcy, and this seems to be an outbreak of that lingering feeling that still exists in some places that either the possession or use of an automobile is one of those conspicuous marks of affluence that singles the user or the possessor of it out for some special legislation at the hands of the governing authorities.

Senator THOMAS. Do you not think that impression is the outgrowth of the personal experience of the customers?

Mr. FITZGERALD. I only have had time to get the figures of this one company. I think it is typical. They operate a very extensive service upon a very small margin. They carefully investigate the character of their employees. They bond them. They are responsible to the patrons of the company. It is not very long since that it was an extrahazardous undertaking, even in a peaceful, well-ordered city like New York, for a person to ride in a taxicab outside of one of the best-lighted thoroughfares of the city, and there are some

places, perhaps, not represented on this committee, where it is still not considered safe to ride in a taxicab under any circumstances. The companies that this tax would affect are the companies that have done more to make respectable, to stabilize and make safe the use of the taxicab, which, in a large city particularly has become essential, than anything else, and if anything is done to destroy them or to eliminate them from the business and to leave only the "bucker" or the "skinner" or the independent, it will bring back the deplorable conditions of a few years since.

On behalf of this industry we ask that that particular provision be eliminated, because it is not believed that, in view of this 2-cent tax on gasoline, the 10 per cent tax on tires and accessories, the tax upon the cars based upon horsepower, and the tax upon cars purchased, there is any justification for an additional tax upon this one particular industry. But the operators and owners of these large concerns have expressed the opinion that, like the rest of the American people at this time, they are willing to make the most supreme sacrifice demanded if it be necessary. And if it be essential to get this revenue they are willing to acquiesce in the tax that has been proposed.

Senator PENROSE. Did you have an opportunity to express your criticisms of this part of the bill to the Ways and Means Committee of the House?

Mr. FITZGERALD. Senator, the first suggestion that this tax was to be imposed was obtained when the bill was published. No suggestion had been made of such a tax. No one knew that such a tax was contemplated. No one went before the committee, and until the committee presented the bill it was not known it was even under consideration. It is one of those things, I imagine, that at the last moment was suggested and incorporated.

Senator PENROSE. It was made at the last moment in an effort to perfect the bill, I suppose.

Mr. FITZGERALD. I suppose it is one of those imperfections that creep in at the last moment, and for the elimination of which it is necessary for us to rely upon the Senate.

Senator GORE. According to your statement, Mr. Fitzgerald, a gross-receipts tax of 5 per cent would be equivalent to a 200 per cent tax on net receipts or net profits. Is that right?

Mr. FITZGERALD. About that. Then, in addition, the condition that applies in New York does not apply elsewhere. The Legislature of New York last year amended the tax law so as to impose a tax upon corporations for the exercise of their franchise of 3 per cent of the net receipts as fixed by the return under the income-tax law. Of course, there would be no net receipts either for excess-profits taxes or income taxes over there. But the margin, after all of these taxes are paid, is very small.

The CHAIRMAN. We will now hear Mr. A. J. Pflaum.

STATEMENT OF MR. A. J. PFLAUM.

Mr. PFLAUM. Mr. Chairman, may I add a word to what Mr. Fitzgerald has said upon this same subject?

Senator GORE. He has made out a case.

Mr. PFLAUM. I arrived in Washington this morning, and, unfortunately, was not able to take part in the conference of the eastern

taxicab owners that was held here last evening. But, representing perhaps the largest taxicab company in the country, I guess the company that originated the cheap taxicab service in the country, the Yellow Cab Co. of Chicago, I want to acquiesce in all that was said by Mr. Fitzgerald on the subject.

The one important thing, as it appeals to me, in connection with the so-called error in the bill as introduced in the House is that, for some unaccountable reason, when they came to this particular section they got away from the original scheme that seems to permeate the entire revenue legislation.

Senator THOMAS. What is that scheme? I would like to know it.

Mr. PFLAUM. The general scheme, as it appears to me from reading the bill, is to raise revenue by a tax on income and profits.

Senator THOMAS. I am very glad to know that there is a scheme in the bill. I have been unable to discover it.

Mr. PFLAUM. Of course, we know it is a bill to raise revenue. The method of raising the revenue is to tax income and to tax profits, and throughout the bill they adhere to that program until they get to this particular section, and then they say, "Instead of taxing profits, we are going to tax gross receipts." On first reading a tax of 5 per cent on gross receipts does not seem like a great deal, but when you stop and work out the proposition, answering the question of the Senator who just asked Mr. Fitzgerald whether it is equivalent of 200 per cent of the net profits, it depends entirely upon what percentage of gross receipts represents your net profits. If you take the case of a company that does a \$2,000,000 business—I am making this statement based upon reports of taxicab operators; they tell me that prior to the war and prior to these extraordinary taxes 10 per cent of the gross receipts was a substantial profit—on \$2,000,000 gross receipts 10 per cent in profit would represent \$200,000 profit. Yet this tax, in addition to the normal corporate tax, in addition to the excess-profits tax, in addition to the excise tax, would levy a tax not of 5 per cent but of 50 per cent of the net income of the corporation. And, surely, it is hard for a person to conceive that the individual who had the clause in mind intended to tax any industry 50 per cent, unless, perhaps, he thought he was taxing some luxury, as they taxed the jewelry business.

Senator THOMAS. I think this tax is in perfect harmony with what may be the scheme of the bill, because it is imposed upon the association or the company doing the business. Our gross-profits and our excess-profits tax are also imposed upon associations or corporations. Do you not see that in each instance the exemption begins where the voter stands?

Mr. PFLAUM. But the tax begins also after they have made the requisite allowance for operating expenses.

Senator THOMAS. Upon the company?

Mr. PFLAUM. Upon the company.

Mr. THOMAS. Not upon the individual?

Mr. PFLAUM. But here they are taxing the company and not the individual.

Mr. THOMAS. Exactly; and that is the same plan for the imposition of the excess-profits and the war-profits taxes.

Mr. PFLAUM. Yes; but when you come to amusements, and other things of that kind, you add the tax on the ticket; and the person

who buys pays. When you come to the excise tax—and we are now discussing excise taxes on commodities, on clothing, wearing apparel, shoes, and everything else—it provides that the purchaser shall pay the tax.

Senator THOMAS. It is things like that that make it impossible for me to see any particular scheme in the bill.

Mr. PFLAUM. One has to try to reason the intent that permeated the mind of the person who drafted this bill. When they came to levy this excess tax upon clothing, wearing apparel, users of theaters, or any other subject that is obligated to pay the tax, the bill specifically provides that the consumer or user or person entertained shall have the tax added to the price. Here is one industry where that can not be done, because we are subject not only to municipal regulation by the city councils of the various cities that pass ordinances but in a great many States of the Union we are subject to State regulation by the State utilities commission. So that every vendor of merchandise has an opportunity of safeguarding himself by raising the prices of his commodities in order to protect himself on the new tax scale, and every one of us in the common walks of life knows from everyday experience that the prices have been raised.

When it comes to this particular industry, nothing can be done toward raising the price unless you go first either to the city council or to the State utilities commission.

Another grave inequality in the scheme is the fact that it exempts persons who operate for public hire two taxicabs, and taxes persons who operate for public hire three taxicabs, so that in the smaller districts if a gentleman starts operating two taxicabs for public hire, and his business prospers, he would not put on a third one, because then he would have to pay 5 per cent of his gross receipts. But he could organize a separate company and put on two more and have four taxicabs, but pay no tax.

Senator GORE. There is a scheme.

Mr. PFLAUM. It is unjust, because it discriminates against taxicab corporations in favor of street car corporations, both of whom are subject to municipal ordinances.

Senator PENROSE. Would it not relieve the situation to permit the Postmaster General to run the taxicab service of the country?

Mr. PFLAUM. Senator, that might help some.

Senator PENROSE. That would be a panacea for all the troubles.

Mr. PFLAUM. Let me give this committee this one additional illustration. Take the smaller community, if you will, where a corporation operates 50 trolley cars and takes in \$2,000,000 in fares. Let us take that as an illustration. You come along and start a taxicab company to carry people in the same community, and operate 50 cabs. The only difference is that one corporation runs its 50 cars on rails, the other corporation runs its 50 cars, with rubber tires, on the paved streets, ignoring the rails. Each company takes in \$2,000,000 in gross receipts. The one company pays not one dollar of special excise tax under this bill, and the other company, because it operates without rails, would have to pay \$100,000 tax. We say that scheme is manifestly unfair. It is discriminatory. It not only discriminates against the corporation that operates taxicabs in favor of the corporation that operates other public utilities, but it discriminates against the

corporation in favor of the individual, the so-called "bucker" or "raker," who operates one, two or more cabs.

The gentlemen I represent from the West have the same patriotic ideas about tax legislation as the gentlemen operating taxicabs in the East. We do not appear before this committee to ask to be relieved from any just tax that we ought to pay. We do not ask this committee to reduce taxes. We ask this committee to equalize the matter, and make it fair. We appreciate that the committee is going to be sorely tried to raise by taxation the gigantic sum of money that is necessary, and we recognize the great number of taxicabs used for public hire throughout the United States of America. Do not single out the corporation. If you are going to tax the industry, tax it, and tax everybody who operates an automobile for public hire, and if it is to be an excise or special tax, then the equitable, just and fair way to tax it is to tax the automobile.

Senator PENROSE. I think the committee fully understands it.

Mr. PFLAUM. That is the very point.

Senator THOMAS. We heard one argument yesterday upon this subject, and we are pretty well informed.

Senator SMOOR. I do not think there is any necessity of taking any more time.

Mr. PFLAUM. That is the sum and substance of it.

The CHAIRMAN. I think the committee will understand it. You remember we had this same question, in a slightly different form, in the last bill. There was a difference between the position of the House and the position of the Senate upon this question in the last bill. I think your fundamental position is probably in line with that of the Senate committee when it framed the last bill; that is, that all excise taxes, if imposed at all, ought to be imposed in such a way that they can be passed on in some way or another, and you contend here, and I think you make a pretty strong case, that it would be difficult, under the circumstances, for this tax in many instances to be passed on.

Mr. PFLAUM. It would be well-nigh impossible.

The CHAIRMAN. You could not very well require the purchaser to pay this additional tax. You could not do it at all on the gross income basis.

Mr. PFLAUM. I think the collection of it would be entailed with so many difficulties that it would be impracticable to enforce the collection of it if the person who rides in the taxicab was to be called upon to pay the excess fare.

(The chairman submitted a letter from Mr. E. C. Finney, which is here printed in full, as follows:)

PETROLEUM.

WASHINGTON, D. C.,

September 20, 1918.

MY DEAR SENATOR: Permit me to call attention to section 1006 of the revenue bill, H. R. 12863, providing for a tax on automobiles. You will note that the tax proposed is \$10 on cars of 23 horsepower or less, \$20 on cars of horsepower between 23 and 30, and \$30 on cars between 30 and 40 horsepower, etc. I venture to suggest that this is not a fair and equitable way of taxing automobiles. It would seem to me that a fairer way would be to place the tax upon the value of the car, making reasonable deductions for age. Under the House bill a car 4 or 5 years old, and of small value, will be taxed exactly the same as a

brand new car. If, however, in the opinion of your committee the tax should be upon horsepower, it would seem to me that it should be laid as are taxes on automobiles in the State of Maryland, namely, so many cents per horsepower. Under the House provision, a man with an automobile of 24 horsepower will pay as much tax as the man with an automobile of 30 horsepower. The man with an automobile of 31 horsepower will pay as much tax as the man with one of 40 horsepower. This is evidently not logical or fair, even from the viewpoint of the House, which seems to be that the tax should be on horsepower because of the use or damage of the roads by the cars, the damage being theoretically, at least, greater as the horsepower increases. If the tax was made 50, 60, or 70 cents per horsepower, you will see that each man would then pay an exact proportion to the power of his car.

Very truly, yours,

E. C. FINNEY.

HON. F. M. SIMMONS,
Chairman Committee on Finance, United States Senate.

The CHAIRMAN. The committee will be pleased at this time to hear Hon. Harry Covington.

STATEMENT OF HON. J. HARRY COVINGTON, OF WASHINGTON, D. C.

MR. COVINGTON. Mr. Chairman, I appear with Mr. Fitzgerald, of the law firm of Fitzgerald, Stapleton & Mahon, of New York, as counsel for the committee on taxation of the National Petroleum War Service Committee. It is not our purpose to go into a general discussion of the pending revenue bill. I, personally, as well as Mr. Fitzgerald, would naturally have a predilection against criticizing generally a bill that emanated from the body in which I served for a considerable length of time. We simply want to call attention very briefly to a rather serious situation that really confronts the country as the result of the method of taxing the producing branch of the oil industry. We apprehend that all of you gentlemen are already in possession of the report on the oil situation that has been transmitted to the Senate as the result of the resolution introduced by Senator Lodge.

SENATOR LODGE. Let me ask you, on that point, one question. Those figures were transmitted by the Fuel Administrator?

MR. COVINGTON. Yes.

SENATOR LODGE. Have you any idea who furnished those figures or on what they were based?

MR. COVINGTON. Senator Lodge, I have not, and I frankly say that in discussing the matter with some of the oil men who are here, they say that they did not furnish them. I am not able, therefore, to vouch for the absolute accuracy of those figures.

But I am able to state to you, from the oil industry itself, that as the result of very carefully tabulated figures gathered in the rather systematic way in which they are accustomed to gather them, it may be said with certainty that there is a very substantial shortage of crude oil, which, of course, is the basis of the entire oil industry. To-day the oil production in the United States is not keeping pace with the demand by a very great deal. There is a daily depletion of 60,000 barrels of crude oil in the reserves, and up to this time the reason that the oil industry has been able to furnish the variety of its products in the quantity that it does, is, of course, the existence of a very considerable reserve supply.

It is not, however, an overstatement, and it is said in all earnestness, and with no desire to draw a gloomy picture to this committee,

that unless in the precarious enterprise of crude-oil production, which does not depend upon anything else except new discovery and new development, there is a fair encouragement of new development, an opportunity for that exploration which makes what is known as the "wildcatter" in the oil world, precisely the same as the "prospector" in the mining world, this country unquestionably, if the figures of the oil producers of the United States are accurate, faces a genuine and serious shortage in crude oil, at a time when we are fast demanding a very much increased supply for the manifold necessities of ourselves and our allies across the seas. The expansion of our own Army and its maintenance abroad alone means a vastly increased demand for fuel oil, lubricating oil, and gasoline.

Senator THOMAS. Of course, you know that is due in a very large degree to the policy of the Government, which prohibits prospecting for oil on the public domain absolutely, and it takes an oil well away from a successful prospector, either at the time of or just before he develops it.

Mr. COVINGTON. Senator, I am not going to have a controversy with you about that, for I believe there is much to be said for the side of the oil men in this matter.

Senator THOMAS. They are now on the point of impounding the proceeds of those oil companies which are producing on the public domain, and have been producing in strict compliance with the requirements of the laws of the United States. We could have plenty of oil if the prospector were permitted, under the laws of the country, to go out on the public domain and take his chances of the hazard and expense, and bring into the market the treasures of oil in the bowels of the earth on the public domain.

Senator PENROSE. Fear is he might make a little money.

Senator THOMAS. That is one fear. But the whole system, beginning some 10 or 12 years ago, and entirely praiseworthy within proper limitations, has gone to such an extreme that to-day the country is upon the verge of an oil shortage, with no apparent prospect of any change in governmental policy.

Mr. COVINGTON. Senator, I do not entirely disagree with you with respect to the policy of preventing the exploitation of oil and minerals alone on the public domain.

Senator THOMAS. I understand that. I simply emphasized it.

Mr. COVINGTON. I think that is a very much debated question, upon which there have been two sides ever since before the time I entered Congress a number of years ago, and perhaps there will be for a good many years hereafter.

Senator THOMAS. I stated it in order to emphasize your argument.

Mr. COVINGTON. You are absolutely right.

Senator THOMAS. There is a double necessity now for encouraging, in every possible way, oil enterprises upon certain parts of the domain of the United States as are still available.

Senator PENROSE. Judge Covington, in connection with Senator Thomas's question, having destroyed individual enterprise, why would it not be a good idea to appropriate \$50,000,000 as a revolving fund to permit the Postmaster General, or the Secretary of the Interior—or the Secretary of the Treasury, if he has time—to develop oil fields?

Mr. COVINGTON. Senator, I hold no brief for the various persons who might want to have \$50,000,000 appropriations from the Treasury, and therefore I would not like to attempt an answer to that question. The Secretary of the Interior has the public domain under his jurisdiction.

Senator LODGE. Judge Covington, there are great quantities of oil shales in the country, are there not?

Mr. COVINGTON. The recent investigations of the Interior Department, caused, I think, by Secretary Lane, have produced a very informing report, made by Mr. Manning, Chief of the Bureau of Mines. That report shows that there are a very great many oil-producing shales in the United States. I do not know enough about the scientific side of the matter of oil production from shales to be able to say whether that presents an opportunity for immediate relief in America. From what Mr. Manning has told me casually I should have a very great hesitancy in saying that it would.

Senator THOMAS. There is oil enough in the shales of Utah and Colorado to supply the world with oil for 500 years, but we are not permitted to develop it.

Mr. COVINGTON. Based on the method of extracting oil from shales in Scotland, where the volume of production from a given unit is much lower than it would be in the United States, if there were a development of the oil shales of Utah and other regions of the arid West, there could undoubtedly be an eventual production that would yield an enormous supply of oil in this country.

But I apprehend I am going to have only a short time, in the hurry and pressure of the Finance Committee, and I will proceed with my argument.

As you gentlemen in the Senate know, production from the oil shales is a method of increase of production that must run the hazard of legislation affecting the public domain. It is idle for me to stand and talk to you gentlemen here about that. Senator Robinson, with whom I served for some time in the House when he was the chairman of the Public Lands Committee, knows what that hazard is. We can hope for no legislation which will open these shale fields at once. That must come from a new method of treating the public domain.

Senator GORE. A crisis will not wait on that sort of thing.

Mr. COVINGTON. You are quite right, Senator. A crisis will not wait for that to develop. You have confronting this country the question of the present depletion of the oil reserves of America, and you have confronting the country the fact that there is a retarding, and a very serious retarding, of the enormous exploration by the "wildcatter" necessary to assure the fields which will maintain production. The men who, really as partners, but for convenience, if you please, form the small corporation to develop the fields in Oklahoma, in Texas, in Wyoming, or in Kansas are greatly discouraged because at this time the method of taxation, the method of treating all over the original investment as income, liable to all the normal taxes and liable to the war-profits tax or the excess-profits tax, takes practically all the gain in the case of a fortunate development. In the few moments that I hope you will be able to give Mr. Fitzgerald, for he collaborated with me on that subject, I am going to leave with him to go rather into detail and emphasize to you the small chances

that are left to any persons who attempt at this time to explore for oil in any of the existing oil fields in the South or West, or in any of the lands of those sections, not on the public domain, which offer favorable prospects for exploration with the idea that there may be oil.

There is one concrete illustration of the situation that I can not resist a reference to. It is in the printed brief we shall file with you, and it is a case where a concern in Oklahoma found itself in the position where the tax which was to be levied upon it under the existing law was so excessive that it could not raise the money to pay it, being a small producing concern engaged in this business of semiwildcatting. It had, however, one piece of property which could be sold, and it was able to get for it \$300,000. But when that sale was made for \$300,000, if it were made, actually it was found that the concern would have to deduct so large a proportion of the \$300,000 to pay the excess-profits tax to the Treasury that then there would be taken from them the entire \$300,000 of physical property owned, and yet there would be a shortage of \$180,000 of the money to pay the taxes owed the Government. So the concern seriously have had under consideration the perfectly enormous proposition, if you come to think about it, of asking the Treasury of the United States to sequester a portion of the physical property of the concern and sell it to pay a tax that can not otherwise be paid because the relation of the invested capital to excess profits of the concern in this hazardous industry is such at the present time that the very moment that there is a sale of developed oil land it is all excess profits.

In this brief which Mr. Fitzgerald and myself have prepared—and I believe I speak for Judge Shea, who is special counsel for the Oklahoma oil producers—there is a specific suggestion that in lieu of the present method of collecting this exorbitant excess-profits or war-profits tax the actual producer be permitted to pay a flat tax, making him in a special class, and that flat tax to be 20 per cent of the actual sale value of the land at the time it is brought to the stage of production, when he can sell it to the concern that is able to develop it and to send the oil into its normal flow of refined product for consumption.

Senator JONES. I just wondered if you would put your remedy in such shape as to enable us to deal generally with extrahazardous enterprises.

Mr. COVINGTON. Senator Jones, of course the thing that characterizes an enterprise as hazardous is so variable that it is very hard to classify industries in the country as normal, hazardous, and extrahazardous. What we do say is that, in so far as the production of crude oil is concerned, there is so special a condition existing in the oil fields of America and so special a condition that is inherent in the matter of oil production, in that the product is a fugitive substance, which has to be searched for and located under the soil, that oil production may fairly be called a special class of industry, entitled to exceptionally favored treatment in the matter of taxing oil-land sales.

Senator JONES. Is that different in principle from the man who mines gold?

Senator PENROSE. Or coal?

Senator JONES. Coal mining, I take it, is not so hazardous as the mining of those other minerals. But you take especially the case where the man is spending some years in developing a gold mine, and through the running of a tunnel or the sinking of a shaft he discovers a rich body of ore.

Mr. COVINGTON. I do not think there is any difference, if you ask me, to the extent that each represents a prospecting hazard.

Senator GORE. If you will let me interrupt you, there is this distinction: A man working a gold mine may work it to the limits of his claim. The man owning an adjacent claim is not affected by it. But if a big concern owns oil leases adjacent to a small concern and the big concern puts down wells near the line the small concern has to put down wells or have its line drained. It loses its property, and if it is not able to finance it, it has it drained, and this tax makes it impossible for small concerns to dispose of their holdings, because the tax takes all the property, and they have to sit by and hold it, whereas if they were permitted to sell to big concerns they could go ahead and wildcat in other communities. But they must develop or else their neighbor will take their substance. That differentiates it to that extent from coal and gold mines, although short-lived mines in large measure are in the same category with oil wells.

Mr. COVINGTON. Senator Jones, what I wanted to impress upon you was simply this, that each of them presents a special situation in exploration and development. Each of them presents a situation that fairly requires special treatment at the hands of a Congress seeking to do equity in the matter of taxing essential enterprises which are by no means stable and in which there are always one or the other financial condition present—an excess loss or an excess profit. Each of them is similar in a certain sense. I take the oil industry, and since I have been examining the situation for the oil producers I have come to find, according to the best statements I can get, that there has been more money lost, startling as that may seem, in the unsuccessful developments of oil fields than there has been made in the successful developments of oil fields.

Senator THOMAS. That is true also of gold and silver and lead and copper.

Mr. COVINGTON. I am not prepared to controvert that.

Senator JONES. You are reaching a point now which I hoped you would bring out. Do you think it advisable that there be some tribunal which shall adjust these profits or values, whatever we may term them, in a way to allow a reasonable return to the owner of the property, or should we in this bill specify the oil industry or the gold-mining industry or other hazardous enterprises, or create a tribunal which shall adjust these taxes on an equitable basis, so far as hazardous enterprises are concerned?

Mr. COVINGTON. Senator, if you could work out a plan for an administrative board composed of men who are specialists in the various fields connected with the exceptional industries with which they shall be expected to deal, and that administrative board would not have delegated to it a portion of the taxing power which might make the entire plan unconstitutional. I should have no hesitancy in saying that all such industries as the oil industry and the mining industry could receive much more intelligent treatment after the thoughtful consideration that would be given it by such board than

could be the result of arbitrary provisions written into a revenue bill with the pressure upon the framers of it. But I do not know whether in the present bill you are able—I have no information, of course, nor has anyone outside this committee room, of the transactions that are going on within it—I do not know whether you are able to provide for such a commission as that. I am a strong believer, and I believe I would speak almost entirely for the oil industry—is not that true, Judge Shea?—I am a strong believer in such a board.

Mr. SHEA. We have recommended it.

Mr. COVINGTON. Judge Shea recommended it, after much thought, in the brief that was filed with the House. That recommendation, in a general way, was based on the fact that the experts selected by the Government, if you please, may be well trusted by any industry that does not want to evade or dodge taxes, but simply wants the Government to deal with eminent fairness toward it.

The CHAIRMAN. This bill creates a special board, as you probably recall.

Mr. COVINGTON. Yes, sir.

The CHAIRMAN. If it were thought wise to delegate to them powers and functions as defined by Senator Jones, that could be done?

Mr. COVINGTON. As a matter of fact, the advisory board provided for in the bill at the present time does not possess a very great degree of power.

The CHAIRMAN. I said if it were thought advisable to delegate to them special powers in these regards it could be done?

Mr. COVINGTON. If you could broaden the powers of an advisory, making it a board of specialists, and permit it to adjust the obvious inequalities and injustices of taxation that must creep into a bill of this sort, I concede it would be far preferable than to attempt to write into such bill a provision to deal with such industries as the oil industry, because they could then make a clear case for the many and widely variable situations before a board which could take the time to find in each case precisely what the situation was.

Senator JONES. It strikes me that one of the fundamental difficulties of the present bill rests right in what you are presenting. I doubt if it is possible in this bill or in any revenue bill to define proper exemptions for the various lines of industry and have it worked out automatically. We all recognize that the banking industry, for instance, not being generally a hazardous enterprise, is perfectly willing to accept a very low rate of earnings on its capital as exempt from a tax. But you go into other enterprises, and they must pay the great profits to compensate them for the risk involved in the business. Whether this can be done by varying the amount of exemptions in the bill as equitably as by a commission to inquire into various lines of industry is a great problem, and, to my mind, the thing which you suggest here is one of the very broad subjects which must be dealt with in this bill.

Mr. COVINGTON. I must speak frankly with you, as this is a very serious matter, the matter of framing so stupendous a revenue bill, and I must say that I do not know what the view might be in the Senate in respect of writing what I think is an ideal statute; that is, a statute drawn in most general terms to effectuate the object and permitting a properly constructed administrative body to do what

the Supreme Court has repeatedly described as "filling in the details."

Senator PENROSE. What assurance have any of us that the taxpayers of the country can get a properly constituted body? Would you consider the professor of Latin and Greek from some college as qualified to pass on the petroleum industry?

Senator ROBINSON. No more than you would a professional politician.

Mr. COVINGTON. That would depend on the man. The personal equation enters into that so largely. But that gets into an abstraction. I should have an abundance of confidence myself, while you might not, that if it were there would be authorized a selection of a commission that would be sufficiently intelligent and sufficiently impartial to administer with fairness and skill the general principles written into law and to do that with absolute justice to all the industries affected. But I realize that such a proposal would probably produce a very serious controversy in the Senate.

Senator PENROSE. I am an optimist, but I do not feel that my optimism is justified by precedents.

Mr. COVINGTON. I perhaps may be even more of an optimist than I have known for a good many years that you are.

The CHAIRMAN. Judge, you have made a suggestion that is worthy of very serious consideration. Whether or not the committee will act upon that suggestion is a matter we can take up and discuss. So you need not discuss that now.

— Mr. COVINGTON. We have filed a brief here dealing with our suggestion. There is another matter I want to call brief attention to. I think it can be dealt with in almost a moment.

In the House bill in the two sections which provide for deductions allowed to individuals in relation to the income tax and for deductions from excess profits in the case of corporations, seemingly because the House was considering a variety of other matters connected with the oil industry they left the provision of law respecting depletion of oil and gas wells in the way that it is in the existing law. The Treasury Decision No. 2448, rendered on February 4, 1917, pointed out that this provision circumscribed their activities in respect of allowance for depletion and seems to recognize that that provision of existing law is in a sense unworkable and unfair in that it only dealt with a deduction for the decrease of the flow of an oil well after it has reached its settled flow and the flush flow has entirely passed away.

We have offered as our second concrete suggestion a very simple provision that has already been adopted by the House with regard to mines. The depletion clause will then read "in the case of mines, oil and gas wells, a reasonable allowance for depletion."

The bill then going on to provide, as it does in many other places, that the Commissioner of Internal Revenue and the Secretary of the Treasury shall promulgate the suitable and necessary rules and regulations to make that provision effective.

The pending bill provides that in the case of mines a reasonable allowance for depletion shall be made. But it does not change the law as it now stands in respect to oil and gas wells, seemingly because there was not a concrete discussion of that particular point in the House. What we ask for in that respect is that mines, oil and

gas wells be brought within the single provision that a reasonable allowance for depletion without statutory restriction shall be made.

Senator GORE. To make it uniform?

Mr. COVINGTON. To make it uniform. It ought to be the law now, and that will be a very simple matter for you gentlemen to correct. The value of the suggested change is this: That the depletion of oil wells is so variable that it is hard to write into a statute a clause that will accurately and arbitrarily provide a method by which in all instances depletion of a well may be calculated with justice to the person who has the capital invested in that well.

The oil and natural gas people are quite content to have the rules and regulations made sufficiently elastic to meet each particular case as it is presented to the Treasury as their measure of remedy. That has already been given to the mine owners of the country.

Senator GORE. This point ought to be kept in mind: That the flow of oil, when taken out of the well, is the taking out of capital. It does not represent profit, but the major portion of it represents capital.

Mr. COVINGTON. This provision is merely for depletion. The Treasury regulations now provide a different method to compute depletion in taking out oil and in taking out ore from mines. When they come to calculate the matter of depletion of an oil well, if the new provision is inserted, then they will have to calculate it with a broad knowledge of the oil field in which the well is located, with the production of that field, with the possibilities, just as you cited a few moments ago that the owners of abutting properties having wells which touch the same pool in the sand will cause depletion. But that can all be taken care of amply by a suitable rule and regulation of the Treasury.

Senator GORE. The point I was making is that the proceeds of oil is not all income; it is mostly capital.

Mr. COVINGTON. Absolutely not income. Most of the proceeds of oil are the returns of capital, and when you get down to the real basis of it there is no profit in an oil well until you get your capital back. And the oil producers will want to submit a provision to be inserted in the bill to deal with their peculiar situation relating to the return of invested capital.

The CHAIRMAN. I think what you are saying with reference to a discriminating differentiation between these two industries is so apparent upon the face of the bill that it must have been a case of oversight.

Mr. COVINGTON. I think, frankly, that it was overlooked in the House.

The CHAIRMAN. A reading of it called to my attention the things you have been referring to, and I think the House overlooked it.

Mr. COVINGTON. I think there is no question about that, that they got into rather an elaborate hearing, which must have covered several days and dealt with other matters.

The CHAIRMAN. I am saying that because I do not think you need to spend any more time on it.

Mr. COVINGTON. In behalf of the manufacturing and refining branches of the oil industry I now desire to bring to the attention of the committee, not by way of protest, but by way of very serious reminder, the fact that while these branches are asking no special con-

sideration whatever in the way of tax legislation for their very large proportion of the total oil industry of the country, in other words, are asking nothing more than is provided in respect to other corporations engaged in industrial enterprises. The gasoline tax as provided in the House bill is a serious departure from the general purpose of that bill.

In the provision for a gasoline tax, while the oil industry does not protest about it, it is felt that it is fair to call to the attention of this committee the fact that the House has called this a tax upon a luxury, when, as a matter of fact, it is unescapable that it is a bald tax upon consumption. If you are going to tax an article in everyday use, which the statistics show is to at least three-quarters of its total consumption used for normal activities that are as essential as the operating of a railroad train, as necessary as the use of coal that is burned in a factory or in a house for heating purposes, that article ought to be taxed with a full appreciation of the fact that it is a consumption tax upon a necessary, which is to be passed along to the consumer as a consumption tax. If the Senate is to have consumption taxes that is an economic matter for them to consider.

Senator GORE. It has the vice of being a tax on a source of industrial power, and the tax multiplies with all the processes of varying use.

Mr. COVINGTON. The gasoline tax does all that. A consumption tax, as the chairman of this committee advisedly stated a few moments ago, if levied at all, is levied as an excise tax, on the theory that it may be diffused in accordance with an economic principle of taxation, the diffusion of taxes, and with the consequent passing of them along to the ultimate consumer. If this one industry, however, is to have a consumption tax levied upon it, which is to be passed along, and after the war there is a continuance of abnormal taxes for a period in order to take care of the great revenues necessary, in part, to liquidate our enormous war debt, there may, nevertheless, be such a curtailment of the uses of oil that there may be a fair supply of oil in the country to meet the needs of a period of reaction and industrial dullness. Then one of the well-known economic laws comes into existence, recognized since the days of Adam Smith, the fact that you can not pass along a consumption tax when the time comes that the competitive distributors of the taxed article have more of their product than the consumer will take. Then the person who has the tax levied upon him in the first instance must pay it all. Therefore, to recognize by silence that the gasoline tax is a tax on a luxury would be to concede the propriety of it as a special tax to be paid by the producer when similar articles are not taxed. The oil industry wants to bear its burdens fully, but it is the producer of a great necessity and taxes ought to be levied upon its product in harmony with a general plan of taxation.

Senator PENROSE. Judge, you have referred to the deficiency in the supply of oil. Why should the effort at Sunday conservation stop at the Mississippi River?

Mr. COVINGTON. Senator, I have no accurate information on that subject.

Senator PENROSE. I did not know but what your studies, which evidently have been very thorough, had led you to give some thought

to that. Is there any reason why the conservation should stop at the Mississippi River?

Mr. COVINGTON. I say I am uninformed about that, Senator.

Senator PENROSE. I would like, Mr. Chairman, to introduce this observation at this time, that the effect of the Sunday law in Pennsylvania has been to cause a loss of at least an extra day among the miners. They have gone home or gone to visit where they desired on Saturday evening and not been able to return until Monday, making a loss in coal production of a very vital and considerable amount, by an order which ought to be thoroughly investigated.

The CHAIRMAN. Judge, you have certainly been talking to us very interestingly, and also very profitably. But we have a good many gentlemen here to be heard.

Mr. COVINGTON. I am ready to stop whenever you say. I have appreciated so thoroughly the rigorous rule in the House of Representatives, the five-minute rule, that it is not a serious hardship to close a discussion at any time. And, in fact, I have concluded what I had to present.

Senator GORE. A consumption tax, according to a well-recognized principle and authority, ought to be on the finished product ready for final consumption and not on a raw material, any crude material, any material partly manufactured. While gasoline is to the refiner a finished material, it is not in the regular course of industry. It is the raw material of those who use it in manufacture.

Mr. COVINGTON. Absolutely, and as such raw material it represents about three-quarters of the entire gasoline product of the country.

Senator GORE. And a tax on gasoline would be to carry this price all the way through all the processes?

Mr. COVINGTON. I might say that there are about 400,000 motor trucks in this country to-day out of a total registration of motor vehicles of 5,000,000, and more than one-third of all the registration is in the 10 rural States of this country west of the Mississippi River, which have not a single great city within them.

Senator McCUMBER. Did you say that about three-quarters of the gasoline is used in industries?

Mr. COVINGTON. I did not say in industries. I said approximately three-quarters, as well as the data can be gathered, is used not for pleasure purposes. I did not mean to characterize industrial uses unless you take a broad classification and say that every essential use is within itself an industrial use. While it is a very difficult thing to get at accurately, I should say that not more than 25 per cent of the gasoline of the country is used for pleasure purposes. Some authorities say as little as 17 per cent is used for pleasure purposes. When I remind you that there are more automobiles registered in your State than there are in this so-called automobile heaven of the District of Columbia I think you catch the significance of my statement.

Senator PENROSE. I simply want to state at this time that I have been greatly impressed with the statement of the judge and intend to ask the committee at a convenient opportunity, and very soon, in connection with these statements, to request the presence of officials of the Fuel Administration Bureau to appear before the committee and explain the exact status of the oil and gasoline supply.

The CHAIRMAN. That is the Senator's privilege if he desires to do it.

Mr. COVINGTON. I would like Mr. Fitzgerald to make a few observations respecting a particular phase of the bill as it affects the oil-producing industry. I want also to thank you for your consideration to me and to those I represent.

The CHAIRMAN. If Mr. Fitzgerald wishes to develop some other phase, of course the committee will hear him, although we have made a rule, Mr. Fitzgerald, not to hear more than two statements with reference to the same matter.

Senator TOWNSEND. Have you something new to present on this subject, Mr. Fitzgerald?

Mr. FITZGERALD. If you only wish to hear two persons, Judge Shea, here representing the midcontinental oil producers, ought to be given an opportunity to be heard.

Senator GORE. I am especially anxious that Judge Shea should be heard.

Mr. FITZGERALD. There is one phase I would like to speak of. But I do not want to take the time if Judge Shea is thus to be prevented from addressing the committee.

The CHAIRMAN. We must place some limitation or we will not get through.

Mr. FITZGERALD. I appreciate that, and if it is the desire of the committee to hear only two persons I think Judge Shea ought to be heard in preference to myself.

The CHAIRMAN. That is a matter between you and Judge Shea.

(The following brief was subsequently submitted by Mr. Covington and is here printed in full, as follows:)

STATEMENT SUBMITTED BY THE SPECIAL COMMITTEE ON TAXATION OF THE NATIONAL PETROLEUM WAR SERVICE COMMITTEE, SUGGESTING MODIFICATIONS OF THE PENDING REVENUE BILL, H. R. 12863, AS IT AFFECTS THE ACTUAL PRODUCTION OF OIL AND NATURAL GAS, BY J. HARRY COVINGTON, FITZGERALD, STAPLETON & MAHON, COUNSEL.

This statement is submitted in behalf of the oil and natural-gas producers of the United States by a special committee on taxation selected by the national petroleum war service committee. While it is prepared at the instance of the oil and natural-gas producers, its purpose is simply to assist the Congress in formulating a revenue law which in its operation will be just to the oil and natural-gas industries at the same time that it causes them to bear their full and fair share of the taxes which all patriotic Americans recognize as necessary to be levied in the present exigency of our Government.

It is proper to state that those concerns engaged in the transportation, manufacturing, and distribution of oil and oil products, and in the transportation and distribution of natural gas are asking no special consideration in respect of the taxes to be levied and collected in the pending revenue bill. Those branches of the oil and natural-gas industries recognize that the comparative situation which they occupy in the present condition of American business make it eminently proper that they should be taxed in the same manner as business generally is to be taxed.

The situation in the producing branch of the oil industry is, however, very precarious. At the present time the United States is drawing upon its crude-oil reserves at the rate of 60,000 barrels a day in order to meet its demands. As the size of our Army increases, with the tremendously increased number of tractors, motor trucks, ambulances, and aeroplanes, it is inevitable that the crude-oil demands of the country will greatly increase.

The oil and natural-gas supply is kept up by new explorations and new developments. If the supply is to be maintained and sufficient fuel oil, lubricants, and gasoline are to be available, those explorations must go on, and

must be encouraged in such a way that the explorer, known as the "wild-catter," will continue his financially hazardous activities with the assurance that all his reward will not be taken from him in the event of success.

As indicative of the actual financial hazard in oil producing, it has been stated by men who are quite familiar with the business that the total sums realized from the sale of oil up to this date would not equal the total expenditures in attempting to produce and in producing the same.

As an illustration of the rapidity with which existing fields show a constantly decreasing production, attention is called to the fact that in 1914-15 the Cushing Pool in Oklahoma was largely developed—a little strip of ground 6 miles wide and 12 miles long. This pool produced at its peak about 350,000 barrels per day of the highest grade oil ever produced in this country in any large quantity. This is considerably more than the entire Mid-Continent field is producing at this time, and the Cushing field is now producing only 55,000 barrels per day.

In 1916-17 the great Augusta and Eldorado fields in Kansas were developed, and at the high point had an enormous production of high-grade oil. This is rapidly falling off, and at the present time there is no field in sight to take the place of these two fields.

The Senate has reliable information as to the gravity of the impending gasoline shortage. The report transmitted by the Fuel Administrator on September 11, 1918, in response to Senate resolution No. 299, indicates a probable shortage by the end of this calendar year of 1,000,000 barrels of gasoline.

It is impracticable to obtain absolutely accurate statements as to the requirements of the Government and commerce for the next calendar year, but some estimates have been made for the present year by competent authorities. In Bulletin No. 14 of the Kansas City Testing Laboratory, 1918 edition, entitled "Petroleum, Asphalt, and Natural Gas," it is stated that the demand on United States refineries for gasoline and naphtha in 1918 has been estimated as follows:

	Million barrels.
Pleasure automobiles	20
Export	15
Commercial auto service	12
United States Army	8
Stationary gasoline engines	8
Other uses	10
Total	73

The number of so-called "pleasure" cars is difficult to determine. A great many cars included in such a classification are used primarily as business necessities and only incidentally for pleasure; others are chiefly for recreation purposes and incidentally for business, although for business to a very considerable extent; while the number in use solely for pleasure is very much less than the total included in the classification of pleasure cars.

Where only a brief time ago automobiles were almost universally regarded as a luxury, and their possession the visible and unmistakable indication of affluence, to-day they are as generally recognized as indispensable factors in the transaction of the complex business of this progressive age.

The total motor vehicle registration of the United States on January 1, 1918, was in round numbers 5,085,000. Of this number there were 1,685,000, or about one-third of the total, automobiles and trucks registered in the 10 purely agricultural and rural States of Iowa, Minnesota, California, Kansas, Texas, Wisconsin, Missouri, Nebraska, North Dakota, and South Dakota.

Moreover, of the total there are in the United States 254,000 motorcycles which, as every one knows, are used almost entirely for utilitarian purposes. There are also 400,000 motor trucks (testimony of Mr. G. M. Graham, chairman National Automobile Chamber of Commerce, motor truck committee, House Hearings, p. 1077) which, of course, are used entirely for essential work.

In view of these statistics, it is fairly certain that the somewhat prevalent belief that a large percentage of the gasoline consumed is used for nonessential and purely recreational purposes is not well founded. While something may be gained by imposing restrictions upon the uses to which gasoline may be put, reliance for the maintenance of a continued and sufficient supply of gasoline must depend upon new discoveries and developments.

It is assumed that the extrahazardous character of the "wild-catter" business in the oil industry is as well established as that of the "prospector" for precious metals. If gas, oil, and precious metals could be located in the same systematic manner that virgin land is cleared, broken, and made productive, there would be no occasion for alarm because of prospective shortages, nor would there be need for special consideration of those engaged in prospecting for such commodities. But "wild-catting" is, indeed, a precarious and uncertain business or occupation. The hope of large rewards from some discovery, which will compensate for a lifetime of effort, is the stimulus which holds men in the occupation. While some attain that which all seek, and by a lucky strike reap substantial returns for the hard years of fruitless effort, most of the "wild-catters," like the prospectors for precious metals, pass out disappointed and with no adequate return for their life's effort and industry.

Under the existing law, and under the proposed law, all incentive is taken from the "wild-catter." The method adopted of treating the difference between the sales price and the amount actually expended to acquire property and develop it to the point where gas or oil is discovered as profits for the year in which the sale is made, has practically stopped sales of newly discovered gas and oil properties.

As illustrating the effect of the operation of the present law, a pending case is startling.

A concern with a nominal capital is subject to a tax of \$240,000 under the existing law. It had not the money to pay the tax. It could sell one parcel of its holdings for \$300,000. The entire proceeds, under the law, would be considered as profits. After disposing of the property, actually part of its capital, for \$300,000, and paying 60 per cent of the price received as taxes, it would still be short \$120,000 to make up its indebtedness of \$240,000, for which it had parted with property of \$300,000 in value.

Consideration of the effect of the proposed law demonstrates how futile it would be to rely upon the operations of the "wild-catter" for a continuance of the gasoline supply.

Take the case of three partners who for convenience incorporate and contribute \$20,000 each to the capital. Assume that they invest the capital in acquiring properties and expend \$40,000 additional in drilling several wells, as a result of which gas or oil is discovered in considerable quantity. If such property were really rich in gas or oil, it would not be unusual for it to have a marketable value of \$1,000,000.

If the discoverers of this gas or oil contemplated disposing of the property, they would face this situation: The difference between the sales price and the invested capital would be considered as profit. This difference would be \$900,000. Under section 312 of the proposed law a specific exemption of \$3,000 would be allowed and an additional sum equal to 10 per cent of the invested capital, amounting to \$10,000, or \$13,000 in all. The balance, \$887,000, would be subject to an 80 per cent tax, aggregating \$709,600. There would be left to the corporation \$177,400. Under the corporation-tax provision of the proposed law (section 230), after the allowance of \$2,000 provided in section 236, there is a tax upon the net income which, with the deduction mentioned, is \$175,400. Assuming that the entire \$175,400 is to be distributed as dividends, there would first be deducted 12 per cent, or \$20,848, leaving \$154,552 to be distributed as dividends. If so distributed, the three partners would receive \$51,517 each, and, under the income-tax provision of the law, would pay \$12,980 each.

Thus, as a result of a transaction involving \$1,000,000, with profits of \$900,000, there would be paid in taxes under the proposed law \$769,394, and each of the three persons engaged in the enterprise would receive \$38,537.

Innumerable illustrations might be presented where the operations of the proposed law would be equally drastic. The one presented is selected because typical. When it is considered that the discovery of such properties is not the common fortune of the explorer; that for every such rich location there are failures numbering in the thousands; that the losses from year to year can not be offset, but must be borne without redress, unless compensated by the unusual and rare discovery—it must be apparent that some special provision must be made to meet such peculiar and unusual conditions.

SPECIAL TAX ON SALES.

Appreciating the necessity of holding out substantial returns to encourage those who continue to explore for gas and oil, the following provision is submitted for the consideration of the committee. Add to section 211:

"(a) In the case of oil and gas wells sold by the individual owner thereof, 20 per cent of the actual sales price shall be paid in lieu of all income surtaxes in the year of sale."

And add to section 336, after the first paragraph, the following: .

"In the case of oil and gas wells sold by the corporation owner thereof 20 per cent of the actual sales price shall be paid in lieu of all war-profits or excess-profits taxes in the year of sale."

The effect of these provisions will be to permit the explorer and discoverer to reap fair returns from discoveries; it will start anew the transfer and exchange of properties ready for development to those capable of utilizing the properties to the most complete beneficial use, and it will still leave the individual and corporate explorer subject to the ordinary income and corporation taxes.

Thoughtful consideration by those whose energies are concentrated to produce the maximum supply of oil and gas, with no desire to aid anyone to escape the onerous burdens which necessarily result from existing conditions, but with keen appreciation of the imperative necessity of stimulating those upon whose continued efforts new sources of gas and oil depend, has resulted in the conviction that what is here proposed is equitable and will be effective.

It may be that some other method to relieve the existing situation, equally effective and no less just to all concerned, may be proposed, but none has been suggested which, in the opinion of those most familiar with the situation and who are most competent to appreciate its peril, as fully and as fairly meets the present emergency as the remedy here proposed.

REASONABLE ALLOWANCE FOR DEPLETION.

The production of oil and natural gas, unlike that of most other businesses, begins to diminish the body of the property from the time of the first sale of oil. This is termed by the Treasury Department "depletion." After the discovery of oil the producer must bring it to the surface. He can not wait; he must produce it or lose it, and his market is fixed. He must produce and sell his oil and gas upon whatever market is available at the time. In the matter of coal, iron, and other minerals not fugitive he can await his convenience to bring them to the surface and market them; but in oil, found as it is in pools, with many wells being sunk upon adjacent property, all drawing from the same reservoir, unless the producer speedily develops and produces he will never realize the full value of his property. Unless the producer, therefore, is permitted to have a fair deduction by way of a "depletion" allowance for the loss in the value of his wells from the production of the oil, and which will thereby give him a return which will have replaced his capital and a fair profit at the time the production ends, he has sustained a loss. This can not be accomplished in each instance by a reasonable allowance for actual reduction in flow of his wells from that of the previous year. The number of wells in the area over the pool, the separate ownership of lands on which are wells drawing from such pool, and the number of new wells which may be sunk by the particular individual on his land, all have such an effect on the total production of the unit upon which "depletion" is calculated that it is impossible to write into law a provision which will meet fairly each case.

A quotation from Treasury Decision 2447, issued February 4, 1917, and construing section 5, subdivision eight, and section 12, subdivision second, each of which relate to "depletion" of oil and gas wells, as such "depletion" must be computed under the act of September 8, 1916, the existing law, shows the limitation of discretion allowed to the Treasury officials in meeting the unusual, widely variable, and often serious cases of oil and gas well depletion. That quotation is as follows:

"Notwithstanding the fact that the drilling of new wells may offset the reduction in the production and flow of the older wells in the field not fully developed, the provision of the law hereinbefore quoted does not authorize and this office can not permit a depletion deduction to be taken so long as the flow and production of the unit, be it a well or group of wells, or the entire territory, is as great during the year for which the return is made as it was for the year immediately preceding."

The section of the law there referred to is reproduced in the pending bill, and to overcome the objection which we have just pointed out, we propose for the consideration of the committee amendments of subdivision (10) of section 214

and of subdivision (9) of section 234, which are identical. These amendments are printed below in comparison with the existing law:

PENDING BILL.

(10) (a).

(9) (a) In the case of oil and gas wells a reasonable allowance for actual reduction in flow and production, to be ascertained not by the flush flow but by the settled production or regular flow; (b) in the case of mines, a reasonable allowance for depletion; (c) in the case of mines, oil and gas wells, a reasonable allowance for depreciation of improvements; such reasonable allowance in all the above cases to be made according to the peculiar conditions in each case and under rules and regulations to be prescribed by the commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee. In the case of a nonresident alien, individual deductions under this paragraph shall be allowed only as to property within the United States.

PROPOSED AMENDMENT.

(10) (a).

(9) (a) In the case of mines, oil and gas wells, a reasonable allowance for depletion; (b) in the case of mines, oil and gas wells, a reasonable allowance for depreciation of improvements; such reasonable allowance in the above cases to be made according to the peculiar conditions in each case and under rules and regulations to be prescribed by the commissioner with the approval of the Secretary. In the case of leases, the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee. In the case of a nonresident alien, individual deductions under this paragraph shall be allowed only as to property within the United States.

This amendment does nothing except place oil and natural gas wells in the same class as mines in so far as "depletion" allowance is concerned. The Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, will simply be authorized to promulgate rules and regulations under which "depletion" allowances will be permitted in the returns of oil and natural gas producers, as the bill now provides in the case of mines. It can not be seriously urged that the conditions of "depletion" are not more uncertain and variable in oil and natural gas wells than in mines. Moreover, the officials of the Treasury will abundantly safeguard the revenue of the country by rules and regulations which do not permit "depletion" allowances in any case in excess of the exigency.

THE GASOLINE TAX.

The special committee on taxation, representing practically the entire oil industry, having already indicated in this statement that the manufacturing and distributing branches of the industry are entirely willing to bear their fair and full share of just and equal taxation, feels that the economic character of the gasoline tax should be presented to your committee so that it may be fully understood:

Under section 902 of Title IX of the House bill, in levying excise taxes, it is provided:

"That there shall be levied, assessed, collected, and paid upon all gasoline, naphtha, and other similar petroleum products, having a flash point below 100° Fahrenheit, as tested by the Taglibue open-cup tester, and suitable for motor power, sold by the manufacturer, refiner, or importer, a tax of 2 cents a wine gallon."

The report of the House committee (H. Rept. No. 767, p. 33) says that:

"In recommending excise taxes in the proposed bill your committee has endeavored to select articles that fall within two classes: (1) Articles that are more or less a luxury because of their nature, and (2) articles that become in the nature of a luxury when sold for more than a fixed price. The purpose of the committee in recommending these taxes is twofold: (1) To provide revenue and (2) to reduce extravagance."

The report, obviously referring to its class (1) "Articles that are more or less a luxury because of their nature," goes on to say, "So far as practicable the committee has placed these taxes upon the manufacturer, producer, or importer."

An examination of section 902 shows that an excise tax is to be levied, assessed, collected, and paid upon all gasoline "sold by the manufacturer, refiner, or importer," so that the House committee undoubtedly proceeded upon the theory that a tax upon gasoline was a tax upon an article which "is more or less a luxury," or, in other words, so largely used for pleasure as to make it a legitimate object of taxation when luxuries are being taxed.

Those engaged in the oil industry do not purpose to invite a controversy over the taxation of articles which may be considered an object of taxation at the present time. They are not seeking to evade or avoid taxation, and are quite willing to have their products bear any tax which ought to be imposed on them in an impartial distribution of the burdens of the present war. No controversy over consumption of taxes is, therefore, to be raised by them. It is unmistakable, however, that the proposed tax on gasoline is a consumption tax.

The well-known economist, David A. Wells (*Theory and Practice of Taxation*, p. 597), says:

"All specific taxation of articles ultimately and necessarily falls on consumption; and the burden of every man, under an equitable system of taxation, and which no effort will enable him to avoid, will be in the exact proportion which his aggregate consumption maintains to the aggregate consumption of the community of which he is a member."

When a tax is laid upon an article at the place of original sale, but in such form as to make it nevertheless a consumption tax, it is, of course, as Wells says, a burden borne by the ultimate consumer. If such a method of taxation, with its inherent infirmities and inequalities, is to be generally adopted, the oil industry of the United States can have little complaint, provided the rate of taxation is fair as compared with the rates on other articles of consumption. But when there is a legislative disavowal of the intention to levy consumption taxes, as there is by the Ways and Means Committee of the House, and the outward form of the tax on the particular article, gasoline, is one which the ordinary consumer may believe was not intended as a consumption tax, then when he finds a taxation burden at least partially passed on to him he feels himself oppressed by the industry producing the article.

This statement has already abundantly demonstrated that gasoline is an article of prime necessity. With three-fourths of the total annual consumption by persons using it in as essential a manner as they use coal, it may well be asked by them why such a single necessary article was selected for consumption taxation. Whatever else they may say or think, the small machine-shop man with his stationary gasoline engine, the farmer with his tractor and his car to deliver produce, the owner and operator of a single motor truck as his vocation, the fisherman with his gasoline boat as his means of livelihood, are none of them to be lulled into a feeling that the tax on gasoline is a tax on a luxury.

Moreover, the present time is one when the demand is beyond the supply of gasoline. A price which assures a profit on crude oil to the producer and on gasoline to the refiner is manifestly assured under economic law. On the other hand, it must be understood that the oil industry is no longer a monopoly; many independent concerns genuinely and fiercely compete for business in the peace-time markets. Last year all the units of the old Standard Oil Co. produced less than 20 per cent of the crude oil, and while as refiners those units produced a larger proportion of gasoline, the other great and small concerns produced a very large share of the total output.

Whenever in a field a strong competition there may be, through enterprise encouraged by fair legislation, with a peaceful country, a supply of gasoline more adequate than now, the acceptance by the oil industry of the claim that the gasoline tax is an excise tax on a luxury and not a consumption tax on a necessity, may leave that industry in the post-war period burdened with a tax which is unequal and which it can not stand. It is submitted, therefore, that the gasoline tax ought to be approached by this committee with a full appreciation of its economic character as a consumption tax.

The CHAIRMAN. The committee will next hear Mr. John J. Shea. Judge, I wish to say that the committee would be glad, if you can, not to have covered ground that has just been gone over by the other gentleman.

STATEMENT OF MR. JOHN J. SHEA, OF TULSA, OKLA., REPRESENTING THE MIDCONTINENTAL OIL AND GAS ASSOCIATION.

Mr. SHEA. I will try as far as possible not to do that:

Senator GORE. I think Judge Shea can give some concrete cases that would illustrate the principles which have been presented.

Mr. SHEA. I represent a voluntary association of producers in the Mid-Continent field, producing about one-half of all the oil produced in the United States, and about 65 per cent of all the high-grade oil.

Senator GORE. You mean producers of the crude oil?

Mr. SHEA. Yes. And I speak only for those who produce at this time. Judge W. H. Gill, of Houston, Tex., representing the Texas, Gulf Coast, and Louisiana Association, also appears with us on the brief we have filed here, and owing to the fact that this hearing is being held a little sooner than we had expected we have not the concrete suggestions for the amendments now, but we wish to make the suggestions of the underlying principles at this time, and within a day or two furnish the concrete amendments that we think will cover the suggestions which we make. We will furnish that in printed form, referring to the title and section of the act as it appears in the House bill.

The CHAIRMAN. When you are ready to furnish that just send it in so that it will be printed as a part of your remarks.

Mr. SHEA. I have here the brief. I want to say by way of preface that since this war came on, and during its continuance, the oil industry of the United States has met every requirement to such an extent that no vessel has ever called at an American port for a cargo of oil, or for oil products, that it was not ready for it at the time. Not only that, but in many instances and particularly in a matter of fuel oil, it has been turned over both to our own nation and to our allies without a price being fixed, leaving the price to be determined in the future. We have met every requirement.

We were urged to drill to the utmost possible extent, and in the year 1917 we did increase the total oil production of the United States 40,000,000 barrels.

Senator GORE. You mean more than it had ever increased.

Mr. SHEA. It increased to a greater extent than it ever had before; that is, to a larger amount, not to a greater percentage than it had in any one year. To do this we were compelled to drill what are known as inside locations—that is, to drill locations that could just as well have been left in reserve—to meet the ordinary demands of business.

Oil supply is kept up by finding new fields. It can be done in no other way. New fields are a matter largely of chance. The only new field at this time in sight producing any crude oil outside of the Wyoming field, is in Texas and known as the Ranger field.

The depth at which oil is found there is 3,400 feet, and a well costs from twenty-five to forty thousand dollars. It takes a long time to drill it. The extent of the field is uncertain, so that production for the next 12 months must be kept up by drilling inside locations on proven or tested property, which would better be left in the ground storage, and it would be better for the general public if it could be. But under this emergency it must be brought to the surface.

Senator PENROSE. Is not the development of the Wyoming field considerably held up, if not practically stopped, even, by legislation pending in Congress?

Mr. SHEA. To some extent. It is also largely hindered by transportation facilities. There is no transportation of oil except by railway at the present time.

Senator PENROSE. Are the railroad facilities entirely adequate?

Mr. SHEA. No, sir. You can not ever find adequate railway facilities for the transportation of crude oil. Crude oil must be transported by pipe lines underground in order to furnish an ample supply. For instance, our Oklahoma oil is transported by almost continuous pipe lines to Bayonne, N. J., to east St. Louis, and to the various refineries throughout the Middle West. It is transported by several pipe lines to the Gulf of Mexico, and there reaches tidewater. You can never find ample transportation for crude oil, in the amount demanded by the public, by railroad transportation. It would be a physical impossibility.

Senator LODGE. I understand when you are speaking about the supply of oil, you are speaking only of the crude oil from the flowing wells. You are not discussing shales?

Mr. SHEA. From the pumping wells as well as from flowing wells.

Senator LODGE. You are not discussing shale oils?

Mr. SHEA. No. There is at this time no method by which shale oil can be produced profitably in this country. It is not being produced now, and in this emergency we must rely on the oil from the sands and the drilling as it is now carried on.

Senator PENROSE. Do the regulations and orders of the Department of the Interior facilitate an easy production of oil?

Mr. SHEA. We have no Government land in our country. Some of the land is under the Department of the Interior, and the regulations have been quite satisfactory for a number of years. They have a very intelligent idea and a very comprehensive view of it, and while we complain about some things in their regulations, generally speaking they are quite satisfactory.

Senator GORE. There are no public domains.

Senator PENROSE. Where there are public domains, are you familiar with the effect of the regulations and orders of the Interior Department?

Mr. SHEA. I know but little about that. Those public domains are largely in Wyoming and California, in the oil-producing fields, and I know little about it. I speak only for our field.

We contend, in the first instance, that there are no war profits in the production of oil. In 1916, in the midst of this war, oil in our field was worth \$1.55 a barrel. In July, 1916, it began to go down, and in October, 1916, it was worth only 90 cents a barrel, right in the midst of this war. The reasons for that was the bringing in of the new field known as the El Dorado and Augusta field. So that it depends largely on discovery. The oil producer may make a large amount of money upon a very cheap oil, and he may make a very small amount on a high-priced oil. But he sells his capital assets from the day he begins producing. Senator Jones a while ago spoke about a comparison with minerals. The difference between oil and minerals is that in the Mid-Continent field 95 per cent of all the oil is produced from leases, either in 80, 60, and frequently 160-acre tracts, seldom a larger tract than 160 acres. I drill a well upon my 160, and you drill a well upon yours. I must immediately drill my property up or my neighbors will get my oil, and when it is

brought to the surface I must sell it upon whatever market I can get, because I have no way of storing it. It is an expensive proposition to furnish the steel storage in the first instance, and evaporation loss through such storage makes it a very difficult matter to make the storage of oil a success.

Senator GORE. Nobody could do that but the big concerns.

Mr. SHEA. Storage of oil is only done through force of circumstances. It is done by the big concerns to guard against shortage in supply and to meet the requirements of the market when the oil being produced from the ground is insufficient to meet it. During the month of August of this year we drew 2,400,000 barrels from storage in one month, at the rate of 80,000 barrels per day. There is in storage in the United States at this time, in tanks and pipe lines, something like 140,000,000 barrels of oil. That is in the entire United States. A large amount of that is in California, too distant to come into this market at a living price. So that our Nation and our allies must depend upon the Mid-Continent field and the fields lying east, the Appalachian fields, and the Texas and Gulf coast, for all fuel oil, gasoline, and lubricants that are used.

Senator GORE. That 140,000,000 includes what is in the pipe lines?

Mr. SHEA. Yes. That is idle oil, filling the pipe lines. You have to keep them full all the time. It is idle all the time.

The CHAIRMAN. You said there are no war profits in the production of oil?

Mr. SHEA. Yes, sir.

The CHAIRMAN. You gave figures at which it was selling in 1916. What was it selling for in 1914?

Mr. SHEA. Early in 1914 it was selling at \$1.05 per barrel. Owing to the Cushing field it went down in 1914 to 40 cents a barrel. It went up in 1915 and 1916, until it was \$1.55 in 1916, and then, owing to the discovery of the El Dorado field, it went down to 90 cents.

The CHAIRMAN. Could you give something like the average price?

Mr. SHEA. In a brief filed with the House committee I have the price of oil by months, which I can furnish.

The CHAIRMAN. I would like to get the average price of oil for four or five years preceding the war in Europe.

Mr. SHEA. I could figure that out, although I have not done so. I could get the average price.

The CHAIRMAN. Suppose you get it.

Mr. SHEA. I will do that.

The CHAIRMAN. You say in 1916 it was selling for \$1.10?

Mr. SHEA. It was \$1.55 in 1916, and then went down to 90 cents that same year.

The CHAIRMAN. What is it selling at now?

Mr. SHEA. \$2.25.

The CHAIRMAN. How do you account for that great increase?

Mr. SHEA. There was increase of demand within our own country and a decreased production, both of which contributed. It will cut both ways.

The CHAIRMAN. You account for the increase by the increase in the demand?

Mr. SHEA. There was an increase in demand.

The CHAIRMAN. An increase in the demand as the result of the war?

Mr. SHEA. Not at all. There was a normal increase in demand each year prior to the war. It was going up very rapidly. The demand for oil was expanding very rapidly.

The CHAIRMAN. That is one of the chief reasons why everything is higher now than before the war—increase of demand.

Mr. SHEA. Probably so. That is, to some extent, true. But a large market for oil has been absolutely cut off by the war. For instance, the market which is practically controlled by American refiners in Germany, largely in Russia, in Austria, and in Turkey and Bulgaria, has all been lost.

The CHAIRMAN. But notwithstanding that diminution, there has been an increase in the demand.

Mr. SHEA. Our figures here show an increase in exports, and there has been, of course, an increase in demand. But there was a normal increase in demand growing year by year prior to the war. There was a very depressed condition in the oil field in 1913.

The CHAIRMAN. You do not think that normal increase in demand would have raised prices in two or three years from \$1.10 to \$2.25?

Mr. SHEA. I think that if we had not had a war oil would have been \$3.50 a barrel to-day; and that is the opinion of men who have kept in complete touch with the business. I have every reason to think that it would have been that. I think that the price of oil depends so largely upon the great flush production from new fields, when a new field comes in it depresses the price, naturally. Take, for instance, to show you the decline, and the influence it has in price, the new wells that are being drilled in the Mid-Continent field now, in the old field, where it is already producing, have an initial production less than one-third of their initial production in 1911, 1912, and 1913.

The CHAIRMAN. Is not that falling off of the production in those lines more than offset by the production in these other lines and the large output?

Mr. SHEA. No, sir; it is not offset. There was not so much marketed, but they were capable of producing a great deal more during those years.

Senator GORE. I presume when a new field is brought in, and a large supply, the price always goes down?

Mr. SHEA. The price always goes down.

Senator GORE. And the price fluctuates violently on that account?

Mr. SHEA. Yes.

Senator GORE. And that makes the average price of oil misleading as compared with average prices in other businesses?

Mr. SHEA. We contend that from the profits on oil you ought to take a period of years and average it. You can not compare the three years, 1915, 1916, and 1917, with the three years 1911, 1912, and 1913.

Senator GORE. On account of the violent fluctuations.

Mr. SHEA. In 1913 we produced a large amount of oil at 40 cents a barrel, and we made money. In addition to this, the material that goes into the oil wells and the labor we put in there costs more than twice as much as it did in the prewar period, prior to 1913.

Again, most people get the idea in speaking of oil wells that all you have to do is to drill a hole and start taking your dividends. There are 200,000 producing oil wells in the United States—and that

is some item of oil wells—that are to-day producing less than one barrel of oil per day.

Senator McCUMBER. Two hundred thousand?

Mr. SHEA. Producing wells—yes—that are producing less than one barrel of oil a day.

Senator McCUMBER. What is the entire number of wells in the United States?

Mr. SHEA. There are about 350,000 wells in the United States.

Senator ROBINSON. What is the total daily output?

Mr. SHEA. About 890,000 barrels. It runs from 800,000 to 1,000,000 barrels. The figure for 1917 was 890,000 barrels. One of the things that we ask relief on is this. Of course, all of you who are informed upon mining business will understand this: The prospector goes out and makes a strike. He may have had 10 years of failure before that. The only thing he can do with that is to sell it to somebody who is able to develop it and run it, and he can sell that at a good price, and he takes that money and goes out prospecting with it again or goes into business. He can not sell now, because under the present law and under the proposed law as it comes from the House all of the profits are held to have accrued during the year in which the sale is made, and as the result of that he must give up practically the whole body of his property in taxes.

Now, I think a discoverer ought to be put on a flat rate, and if he makes a sale he ought to pay 20 per cent, say, of his profits in tax. Of course, when that money goes out into circulation it is at once subject to the income tax and it brings new money in and keeps things going.

It is not fair to put the oil business on the same basis as banking, manufacturing, commerce, and other going industries. Their property is worth a little more at the end of every year, while ours is worth a great deal less every year.

Senator GORE. In the other businesses you can make some calculation, you have some basis on which to depend, but in the oil business it is purely a gamble and speculation as to where you will find oil?

Mr. SHEA. Yes; of course.

Senator GORE. Could you give us any information as to the average life of an oil well?

Mr. SHEA. Yes. Speaking of the Mid-Continent field, 35 to 50 per cent of all the oil a well ever produces is taken out the first year. During the remaining two years there would be 25 per cent more. There are various estimates of that—from 70 to 80 it runs, and I am calling it 75. At the end of three years you have 75 per cent of the oil out of the well that you will ever get out of it, and the remaining 25 per cent, or probably 20 per cent, to be more conservative, is taken out by pumping through a period of years, and it comes very slowly. It finally comes to the point where it is no longer profitable to pump, and then the property is abandoned. My own experience in the Mid-Continent field is that 80 per cent is taken out the first three years, and the rest will probably go over a period of eight or nine years. In the Texas and Gulf Coast field, eight months in the life of the wells in some of the districts. They have to be worked over, at great expense, in order to keep them going on and producing the remainder of the oil that is in the sand.

In the Pennsylvania field there have been some very long-lived wells. I know some wells that have been pumping for 40 years, but they only pump them every other Saturday and measure the output in gallons. It is very small.

The CHAIRMAN. That is the only thing they do on a small scale in Pennsylvania, then?

Mr. SHEA. I am speaking now about the remaining percentage of the oil in the well. It is spread over a long period of years, and it finally gets so expensive to bring it to the surface that you must abandon it, because of the small yield and great expense.

Now, we call attention to section 326 of the House bill, on invested capital. That reads as follows—one of the provisions, section (b), I think it is [reading]:

Actual cash value of tangible property other than cash bona fide paid in for stock or shares at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor.

A great number of small concerns, incorporated for the matter of convenience throughout our country, have exchanged their property for stock. I know of one instance where \$600,000 worth of property was exchanged for \$100,000 of stock. They only got a \$100,000 of invested capital under that rule.

In the case of a corporation issuing stock with no par value it gets the full value of such property. In case it turned over \$100,000 worth of property for stock and issued \$1,000,000, the law provides that the Treasury shall ascertain and cut it down to the actual value. The rule ought to be that in all cases the actual value of the property turned over, regardless of the stock issued, whether it is more or less, shall be the invested capital. It is only just and right.

Prior to the excess-profits tax law last year, the capital did not enter into the amount of tax to be paid. It was a matter of convenience. Three men would get together: they owned a property and wanted to turn the property over to a corporation, because it was a convenient way to do business, and they turned over the property and took a nominal amount of stock for the same in equal shares. They ought to get only the actual, fair market value of the property at the time it was turned in for stock and there are hundreds of corporations organized that way where the par value stock did not enter much into it. I know of two corporations in which I am slightly interested, where some of my friends have \$25,000 worth of capital stock and the property is worth, I expect, a couple of hundred thousand dollars, and was worth that when it was turned over.

I know of one corporation having \$7,000 of stock and they turned over \$400,000 of property to the corporation in exchange for its stock. There was no purpose to evade. It was a matter of convenience. In Oklahoma there is a gross production tax on oil, and the value of the stock or property had no connection with the amount of tax; when the Government came around it took the market value of the stock for the stock tax, and this particular property was taxed at a value of \$800,000; so that they ought to have the actual value of the actual, physical property that is turned over to the corporation for stock at the time of the transaction.

Senator GORE. That is the rule under the corporation-excise tax of 1909?

Mr. SHEA. Yes.

Senator GORE. The actual value of the property is what counts and not the value of the stock.

Mr. SHEA. Yes; they do not pay any attention to the actual amount of stock outstanding.

Senator GORE. Is not that true with respect to the existing law in regard to corporations organized since January, 1914?

Mr. SHEA. Yes. This would not involve any difficulty. It would not make any more work for anybody. If a corporation is overcapitalized we will have to find the valuation so as to put it on the tax basis, and it ought to be the actual value of property when turned in for stock.

And, gentlemen, I want to call attention in that connection to the fact that it is extremely easy to find the value of oil property. It is the basis on which it is bought and sold. We buy an oil property on the theory that it will pay us back in three to five years, in an old, settled field. With that in view it is very easy to determine values. The burden is on the taxpayer to show the value to the satisfaction of the Treasury Department. We ought to have that relief and that provision in the bill. "But in no case to exceed the par value of the original stock or shares specifically issued therefor" should be stricken out.

Senator GORE. That provision that you suggest to be stricken out is not in the law with respect to corporations now, organized since January, 1914?

Mr. SHEA. Yes, sir.

Senator GORE. And you are insisting that the law applicable to corporations organized since 1914 should be brought forward in this section?

Mr. SHEA. Yes, sir. The old law says this: That in corporations organized before January, 1914, the par value of the stock or the value of the property exchanged for it, whichever is lower, must be taken as invested capital, those organized since 1914 the actual value of the property exchanged for stock; and the latter ought to be the rule in all cases. The rule of the law is that whatever a man owned when this income tax began in 1913 was his, and that is the starting point and the basis from which he should start.

The CHAIRMAN. I think the committee understand your point on that.

Mr. SHEA. Yes; then I will not take up any more time on it.

The CHAIRMAN. That is undoubtedly a question we will have to consider.

Senator GORE. I do not know whether Judge Shea has it in his mind or not, but if you have, I wish you would state a concrete case. You spoke of this case where the stock of the corporation was \$100,000 and the property was worth \$600,000. Can you state how that would apply to the pending bill?

Mr. SHEA. Yes; here are two properties that were turned over to a corporation formed by the owners themselves in which they each owned one-half, and the property has a market value of \$600,000, and \$100,000 par value of stock issued for the property.

Senator GORE. These are actual facts?

Mr. SHEA. This is an actual fact. They turned over \$600,000 worth of property to their corporation for \$100,000 par value stock, and each of them took one-half of the stock. When they came to pay their tax, here is what would happen to them: they would get on the **profits tax a 10 per cent deduction on their \$100,000 worth of stock** when they were really entitled to a deduction on \$600,000, the value of the property. When you come to the depletion of their property, they would get their depletion allowance on \$100,000 instead of on \$600,000. The result would be that they would pay vastly more taxes than they ought to pay, and more than people fully capitalized would pay. In the first place, they should have a deduction of \$60,000, instead of \$10,000, that means 10 per cent on \$600,000 before they would have reached the war tax.

Now, the Government in the past has encouraged conservative capitalization. It urged it upon people. The States urged it upon people. We were encouraged to do these things and now, having done them, we are penalized for being good.

Senator PENROSE. They put a premium on watered stock?

Mr. SHEA. Yes, sir; they put a premium on watered stock.

Senator GORE. Are you familiar with two instances in a State, of one concern capitalized at only about \$8,000,000 and the other at \$75,000,000?

Mr. SHEA. Yes; I know of a case under the old law where two concerns purchased property in adjoining sections, one concern capitalized at \$20,000 and the other at \$50,000,000, and they purchased exactly the same amount of land, and the \$50,000,000 concern did not pay any tax, under the old law, and the other concern under the law would pay \$600,000. They produced the same amount of oil. Now, these are inequalities. We only complain of the inequality. We do not care anything about the rate of taxation you put on us at all, so long as we can live and get through and keep going and are put on an equality with other industries. We do not want to have our business stopped. In conversation with Mr. Requa the other day—I presume he will be before you; he is the oil man of the Fuel Administration—he said that the result of this tax will be that it will not dry up the source of the oil, but it will result in oil being produced by the larger companies that can spread their losses over the whole field, and the smaller operators will be driven to the wall, and in the happening of the very thing that the Government has sought to prevent, namely, the gathering of all these great properties into the hands of a few large concerns.

Senator LODGE. Was not Mr. Requa, before he came into the administration, an oil operator?

Mr. SHEA. Yes, sir.

Senator LODGE. In California?

Mr. SHEA. Yes; in California. Now, we think that the deduction for the oil producing—we only speak now of the production of oil—should be 15 per cent. It should be in proportion to the cost, of the money you put into the business. You can not get money to go into the oil business on the promise of the same returns that it will have in banking, manufacturing, merchandising, or general business, because of the great hazard connected with the industry.

Senator PENROSE. Can you give me any information as to why the conservation of oil in the order recently made, should have stopped at the Mississippi River? I was curious to know what intangible thought was floating through the minds of those responsible for the order, that induced that reference to the Mississippi River.

Mr. SHEA. I presume that the transportation was what they had in mind, the transportation facilities being limited in the oil, and the fact that most of the gasoline which is used east of the Mississippi comes from west of the Mississippi River, the idea was, that the transportation being shorter and in many cases not being necessary at all, it being sold where it is produced. I suppose that was the idea.

Senator PENROSE. Gasoline is transported on the railroads?

Mr. SHEA. Yes, very largely.

Senator PENROSE. Then it is due to the breakdown of the railroad system rather than to the scarcity of gasoline?

Mr. SHEA. I would not say that there was a breakdown in the transportation of gasoline. I think it has been much improved under Government administration.

Senator PENROSE. It apparently was not adequate.

Mr. SHEA. No, sir; I do not know that it is entirely adequate; but formerly from Tulsa, where I live, it took 40 to 60 days to get your empty tank car back to your factory when it was sent as far east as Chicago, 800 miles. Now we are getting them back in 15 days. So that I think that the transportation of gasoline over the railroads has been greatly improved under this Government administration.

Senator PENROSE. At that particular point?

Mr. SHEA. I only speak for that particular point. The refineries who make gasoline own their own tank cars, and use them in transportation over the railroads, and they have had in the past very great difficulty in getting them back; but we are not having that now, but I think it is largely due to the fact that freight has been given the right of way over everything.

Senator GORE. You were discussing depletion, Judge.

Mr. SHEA. Yes. I agree with Judge Covington on that, and I also agree with the suggestion made by Senator Jones, that there ought to be a board with larger powers than the board is given under the House bill. The English law provides their board with vast powers. They have the power to classify business. For instance, the English law classifies the hazardous industries and gives them a larger rate. For instance, gold mining gets a deduction of 22½ per cent, and others proportionately, and this board of review under the English law has vast power, power to correct inequalities and discriminations, and if a board was clothed with power sufficient to do that, it could probably remedy these things in the administration of the law. At the present time, under the law, there is a board provided, but it is simply advisory, apparently, and has no defined powers.

Senator GORE. There is a fundamental difference between the oil business and the businesses you have enumerated, and your contention is that it is a fundamental difference which ought to be taken into account, and that things that are different ought not to be treated alike.

Mr. SHEA. They ought not to be treated alike. Of course we are going on producing, and will produce at a loss, if necessary. We will produce at a loss as long as the Government needs the product.

Senator GORE. And that notwithstanding that instead of producing at a loss and exhausting your oil you might keep the oil in the ground?

Mr. SHEA. Yes; I am producing oil notwithstanding that I am paying a tax of 80 per cent, and I can drill a new well in a new field and get a lot of oil out of it, but the moment I do that I will immediately have to pay 80 per cent on that new well to the Government, and at the end of the war I will have neither money nor property left. What would be the natural thing for a man to do under those circumstances? He would naturally let the oil stay there. He will not do this under existing conditions because he is going to produce and let the Government have all of the oil that is necessary for its purposes; but they may not be all patriotic enough to do this, and the supply must be kept up and the burden will fall on the most patriotic. We are going to stand for whatever you gentlemen in your wisdom see fit to do; but we do ask that you give consideration to our business in the matter, not for the purpose of escaping taxation, but in order that it may be justly taxed; and in doing that we believe you ought to take into consideration the risk and hazard of the business.

Senator GORE. There are two other points that I would like to have you touch on. One is the difficulty of selling property.

Mr. SHEA. We can not sell property at all. It is absolutely stopped.

Senator GORE. Does that restrict development?

Mr. SHEA. Yes, of course, because the ordinary oil produce depends on his sales. He gets a property and gets it started and he always wants to sell it and take the money to prospect with again. It has absolutely stopped sales.

Senator GORE. Was there not a case down there where they figured they could stand a tax of half a million dollars if they were permitted to sell?

Mr. SHEA. Yes; the report was made to the Treasury that a sale was about to be made, and they were willing to pay a tax of half a million dollars to the Government, but there was no way they could do that.

Senator PENROSE. You could not run those short-line railroads either if the Government had not taken them over. A vast amount of property has been destroyed.

Mr. SHEA. Yes. Of course in the sale of a big property where there is a great investment that is anomalous.

Senator PENROSE. I know millions of dollars have been wiped out by short-line railroads going into the scrap heap.

Mr. SHEA. I have no information on that subject.

Senator LODGE. You explained the fact that there was no restriction west of the Mississippi River by saying that the oil was so much more accessible there. Of course, there must be some long hauls; but at the same time you also said that the transportation had been so improved that it was very accessible now in the East.

Mr. SHEA. Yes, sir.

Senator LODGE. So that the transportation has nothing to do with the eastern restriction?

Mr. SHEA. I only know the reason that I saw stated why it was limited to east of the Mississippi River. I do not know that the transportation is entirely adequate, even now. I say it has been improved so far as gasoline from our district is concerned.

Senator LODGE. The restriction east of the Mississippi was not made to save the transportation, because the transportation is so good that it is not necessary!

Mr. SHEA. The transportation goes clear through to the East.

Senator LODGE. Yes, I understand; and I take it that Chicago is not the only point where the transportation is good.

Mr. SHEA. No, sir.

Senator LODGE. It must be good everywhere.

Mr. SHEA. I presume so. I do not know about that.

Senator LODGE. What I am trying to get at is, when transportation in the East was restricted it was done to save oil, was it not?

Mr. SHEA. Yes, sir.

Senator LODGE. Why is not the saving of oil in one part of the country just as good as in the other?

Mr. SHEA. I am not particularly for that order in any event. I do not much believe in the order of Sunday closing. I am not defending that in any way. There is just one more matter I want to call attention to.

The CHAIRMAN. Before you leave that. You said no sales were being made now. You had reference to sales of oil properties?

Mr. SHEA. Yes, sir.

The CHAIRMAN. I thought you did.

Mr. SHEA. The law absolutely prohibits it, because the tendency is to treat all of the difference between cost and sale price as income during the taxable year. That is the regulation as it exists.

Senator LODGE. As a business man, you realize that you can not sell anything in the United States to-day for anything near its value?

The CHAIRMAN. You do not mean that, do you?

Senator LODGE. I make that statement absolutely, and Judge Shea agrees with me.

The CHAIRMAN. I do not understand you mean to say that you can not sell anything in the United States to-day and at a profit. I understood that things were selling at bigger profits to-day.

I am not saying anything about matters that I am not familiar with, but here in Washington they are selling houses at a very big profit.

Senator LODGE. Washington is wholly exceptional.

The CHAIRMAN. In my section of the country they are selling lands at very much more than they could have sold them for before the war.

Mr. SHEA. He can not sell his property because the profit is so great in it that it would practically all be taken away from him in taxes under the existing law.

The CHAIRMAN. You have given your reasons for the statement you have made that you can not now sell oil properties.

Mr. SHEA. Yes, sir.

Senator PENROSE. Or anything else.

Mr. SHEA. Now, one more question and I am through.

The CHAIRMAN. Did you mean to say that you could not sell anything else in this country?

Mr. SHEA. No; I am speaking of oil property, and particularly new discoveries.

Senator JONES of New Mexico. And the reason that they can not sell now is because the tax would be so high on the apparent profit in the transaction?

Senator PENROSE. Does that apply to other sales?

Mr. SHEA. It does apply to other things, but not with the force with which it applies to oil, because the apparent profit in oil is much greater, although it may actually represent many years of toil, which can not be estimated.

Senator LODGE. You can not sell at a profit because the tax is so heavy. You can sell almost anything at a loss.

Mr. SHEA. Oh, you can sell anything to-day at a loss.

Senator GORE. I wish you would develop this point. Take the case where a man invests \$100,000 in a year and loses it all and then the next year he makes a strike.

Mr. SHEA. Yes; that is a common case.

Senator GORE. I wish you would make a statement on that to the committee.

Mr. SHEA. That is, when a man starts out and has losses this year and has no profits against which to offset them if he makes a profit next year he is not permitted to offset those losses against his profit. That money lost should be capitalized; that is, it should be entered as invested capital, and let it be carried over into the invested-capital account and treated as invested capital so that it may be protected. At present that is not so.

Senator McCUMBER. And there are a vast number who started in business a number of years ago and have run for eight or nine years without getting any return.

Mr. SHEA. I think at the beginning of the law would be the time; for instance, 1917.

The CHAIRMAN. The time for our adjournment or our recess has arrived.

Mr. SHEA. I would like to have 10 minutes more, Mr. Chairman, if I might, later. You can adjourn now and I will take it when you meet again.

The CHAIRMAN. I would rather stay here and let you finish it now, so far as I am concerned. We have been very liberal to you in the matter of time.

Mr. SHEA. The oil business, Mr. Chairman, is probably the fifth business in the United States.

The CHAIRMAN. If you feel like you must have 10 minutes more to make yourself clear and present your views fully, we will give it to you when we meet again.

Mr. SHEA. All right; that will be satisfactory.

(The chairman at this point submitted a letter from Mr. Walter E. Kelley, relating to tax on oil, which is here printed in full as follows:)

SEPTEMBER 19, 1918.

HON. F. M. SIMMONS,

Chairman Finance Committee, United States Senate.

DEAR SENATOR: I submit for the consideration of your committee a few concrete suggestions in regard to the revenue bill as it affects the production of crude petroleum. The peculiar nature of the business will not be touched upon, for that has been covered in the record before the House Committee on Ways and Means at pages 437 to 544, which you have undoubtedly read.

The history of the oil business shows that the producing fields of the United States have practically all been discovered by the operators or operating companies unaffiliated with the great producing, refining, and marketing corporations. This prospecting is accompanied by great financial hazard, and the prospectors, or "wildcatters," as they are termed in the industry, rely on the return from one successful venture to repay them for all their previous losses.

Under the revenue act as now framed the losses incurred in drilling dry holes are allowed to be deducted from the income for the taxable year, and this same provision has existed in the previous income-tax laws, but the difficulty is that, while the prospecting is going on, and until a productive tract is discovered, there is no income from which this deduction can be made, and therefore the provision is purely academic in many cases.

The Government will not suffer any material loss of revenue from a correction of this situation, for all of the big companies have shown a profit for many years and have in consequence already received the benefit of the deduction.

It seems essential, however, that some amendment be incorporated in the bill the effect of which will be to allow the prospector to receive back out of his earnings for the taxable year an amount equivalent to the losses not already deducted from income in previous years. An amendment in substantially the following form, under the heading of "Deductions allowed," would accomplish this result: "In the case of oil and gas wells all losses sustained through the drilling of dry holes from January 1, 1911, not previously deducted from net income for the year in which incurred."

The date January 1, 1911, is suggested as a reasonable one, inasmuch as it is the beginning of the "prewar period" under the excess and war profits provisions occurring later in the bill.

Consequently any losses sustained from that date on would have a direct relation to the amount to be paid as a war-profits or excess-profits tax as well as that to be paid as an income tax.

The suggested amendment, if adopted, will result in some reduction in the taxes of the particular operators affected by it, but this reduction will be much more than compensated for by the revenue which will accrue in 1919 from the productive wells which will be discovered as a result of the allowance being made. An alternative method of dealing with the losses of the prospector during his unsuccessful years would be to permit the addition of the losses not previously deducted to the value of the productive property finally discovered by considering them in the nature of investment.

Thus the total amount upon which the depletion of the productive property would be computed would be larger and the losses would finally be returned in this manner.

I realize that the Congress is confronted with the necessity of raising a huge sum and that suggestions which carry with them even a slight reduction in the total realization are not favored.

However, there is the revenue of 1919 to think of, and also the future production of crude petroleum, both of which will be jeopardized unless reasonable allowances are now made.

The existing stocks above ground are being drawn upon more and more, and new fields must be found if the demand is to be met, for the natural decline in the production of old wells can only be offset by the drilling of new ones.

Another suggestion which I trust may be adopted is in respect to the deduction for depletion of oil wells.

The bill as now framed allows the depletion to be based upon the "settled" production, but eliminates the "flush" production from consideration in computing it. This is a fallacy and is wholly unjust.

An oil well in the early part of its life produces at a much higher rate than at a later period, for when a well is drilled the release of the gas, coupled with the rock pressure and other underground conditions, causes the oil to be expelled from the sand with considerable force for a time. The production so obtained is called the "flush production." After a short period, varying in length in different fields, the production of the well suffers an abrupt decline, and from that time on the production is said to be "settled."

There is only so much oil in the underground reservoir to begin with, however, and whenever a well produces a barrel of oil the reservoir is depleted by just that amount. It is obvious that this depletion results quite as much from the flush production as from the settled production, and it is inequitable not to allow this flush production to be considered in the computation.

There has never to my knowledge been a good reason advanced for restricting this basis to the settled production, and from every standpoint of accounting, sound business principles, and equity the flush production ought to be allowed to be taken into consideration.

An amendment as follows, to be substituted for the present language in section 214a, 10(a), and the similar language in section 234a, 9(a) would accomplish this result: "In the case of oil and gas wells a reasonable allowance for the depletion of the underground deposit; * * *."

That is really what is being depleted, and, while it is undoubtedly the intent of the Ways and Means Committee of the House to make allowance therefor, the reference to "reduction in flow and production" is, in the sections above referred to, somewhat confusing.

If, however, it is felt that the general language of these sections should not be changed the consideration of the flush production can still be provided for by the elimination of the words, "to be ascertained not by the flush flow but by the settled production or regular flow."

I realize that Congress is not disposed to single out any industry for special relief, but the conditions encountered in the drilling for crude petroleum are so unique and so utterly dissimilar from those in any other business that some reasonable exceptions should be made.

The suggestions made herein, if adopted will not result in any reduction of the ultimate amount to be obtained from the oil-producing industry. On the contrary their effect will be to permit the development of new fields, with the consequent increase in production and revenue which will result therefrom.

The average producer is frankly apprehensive as to the effect of the bill in its present form, and there seems to be no doubt that unless relief is given a considerable slump in production will result.

The very vital necessity for crude petroleum in our war program would make this decline nothing short of a calamity. I am told that representatives of the national petroleum war service committee appeared before your committee last week and submitted certain recommendations on this general subject. If their testimony has been printed, will you be kind enough to have the clerk send me a copy of it?

Respectfully,

WALTER E. KELLEY.

BRIEF OF MR. LEE WILLIAMS, OF NORFOLK, VA.

(Mr. Lee Williams, an attorney of Norfolk, Va., introduced by Senator Martin, not having the time to remain to be heard on account of being a member of his local exemption board, desired leave to file a brief, which is here printed in full in the record, as follows:)

Proposed amendment to excess-profits tax law in respect of the ascertainment of net income for the purpose of excess-profits taxation.

It is proposed that at the end of the first paragraph of section 206 of the act approved October 3, 1917, the period after the word "deducted" shall be changed to a colon and the following clause added:

"*Provided*, That for the purpose of ascertaining the gain derived from the sale of property, real, personal, or mixed, acquired before January first, nineteen hundred and seventeen, the fair market price or value of such property as of January first, nineteen hundred and seventeen, shall be the basis for determining the amount of such gain derived; or, at the option of the Commissioner of Internal Revenue, the amount of such gain shall be such proportion of the difference between the selling price and the purchase price as the period from and including January first, nineteen hundred and seventeen, to the date of sale bears to the whole period elapsing between the date of purchase and the date of sale."

DISCUSSION OF AMENDMENT.

This amendment is designed for the purpose of putting the net income derived from the sale of property, real or personal, upon the same basis as other net income subject to the excess-profits tax. By section 200 of the act of October 3, 1917, giving definitions for the purpose of excess-profits taxation, it is provided that the first taxable year shall be the year ending December 31, 1917

(with certain exceptions as to companies fixing their own fiscal years, not material here). It results that the calendar year 1917 was the first year the profits in which were intended to be subjected to excess-profits taxation. It is understood, however, that the claim is made by certain officials of the Internal-Revenue Department that in the case of the sale of property, real or personal, in 1917, or subsequent years, the net income for the purpose of excess-profits taxation is the difference between the selling price and the purchase price, if the property was purchased on or after March 1, 1913, or if the property was purchased prior to that date, that the net income is the difference between the selling price and the fair value as of March 1, 1913. By this construction any increment in the value of the property between March 1, 1913, or the date of purchase, as the case may be, and December 31, 1917, is subject to excess-profits taxation, although the excess-profits law expressly purports to tax only income derived on or after January 1, 1917.

The substantial result of this is that this class of profits is subjected to excess-profits taxation for 3 years and 10 months—that is, the period from and after March 1, 1913, to December 31, 1916, for which period no other class of profits is subject to such taxation. This result is clearly inequitable and is not believed to have been intended by the Congress. The amendment above set out is intended to correct this inequality and, as stated, to place this class of profits on the same basis as other profits. The basis of the construction of the present law by the officials of the Internal-Revenue Department is understood to be the language in clause (c) of the first paragraph of section 206, providing that for the purposes of the excess-profits tax title the net income of a corporation shall be ascertained and determined "for the taxable year upon the same basis and in the same manner as provided in Title I of the act" of September 8, 1916, with an exception not material here. This construction of this language is not believed to be correct and is arbitrary and oppressive. It is true the act of September 8, 1916, provides that for the purpose of ascertaining the gain derived from the sale of property the fair market price or value of the property as of March 1, 1913, shall be the basis. (See sec. 2, clause (c), of the act approved Sept. 8, 1916.) But we must consider the purpose and meaning of the clause in the act of September 8, 1916, just referred to. The income-tax system of the Government became effective March 1, 1913. From and after that date all income from whatever source derived was subject to taxation, and before that date such income was not subject to taxation. Accordingly, in legislating as to income taxation the Congress had in mind that all income derived since March 1, 1913, was to be taxed. It might have been fairer to have provided for the prorating of this income in cases of sales of property between the several years elapsing from March 1, 1913, to the date of sale, and then to tax each year's income at the rates applicable to that particular year, and we do not believe there is anything in clause (c) that would have prevented such an administrative interpretation of the law by the Internal-Revenue Department.

However this may be, the point we wish to emphasize is that a provision that net income for excess-profits tax purposes shall be ascertained on the same basis and in the same manner as income for income-tax purposes relates rather to the basis and manner of ascertaining the income than to the period during which the income may have accrued. In other words, it would be proper to ascertain the income arising from the sale of property for purposes of excess-profits taxation on the basis of the difference between the selling price and the fair value of the property at the date the excess-profits tax law began to operate (Jan. 1, 1917), or such income might have been ascertained in the same manner as income was ascertained for income-tax purposes, prorating it, however, so that only such proportion of the income would be taxed as the period from January 1, 1917, to the date of sale bore to the period from March 1, 1913, to the date of sale. It does not seem to us that this provision for the ascertainment of net income for excess-profits tax purposes should be allowed to override the express statement that the first taxable year was the year ending December 31, 1917, or to bring about the inequalities involved in subjecting this class of profits to a greater tax liability than other classes of profits.

At all events, if the existing law has been correctly construed by the internal-revenue officials above referred to, it is time that the law should be changed.

The proposed amendment in its first clause is taken verbatim from section 2, clause C, of the income-tax law of September 8, 1916, except that the date, March 1, 1913, is changed to January 1, 1917, so as to give effect to the

provision that the first taxable year should be that ending December 31, 1917. The amendment, however, goes further than this in the interest of the United States by providing that at the option of the Commissioner of Internal Revenue the income may be ascertained by taking the entire profit on the transaction and taxing such proportion of that profit as the period from January 1, 1917, to the date of sale bears to the whole period between the date of purchase and the date of sale. This clause might be useful in case there was difficulty in determining the fair value of the property as of December 31, 1916, or in case the Commissioner of Internal Revenue believed that the value returned by the taxpayer for December 31, 1916, was too high. The amendment, therefore, gives a double protection to the United States in this respect.

At 1.02 o'clock p. m. the subcommittee took a recess until 3 o'clock p. m.

AFTER RECESS.

The subcommittee reassembled at 3 o'clock p. m., pursuant to the taking of the recess.

The CHAIRMAN. You may proceed, Judge Shea.

STATEMENT OF MR. JOHN J. SHEA—Resumed.

Mr. SHEA. I will only take a moment more of your time, gentlemen. I want to call your attention to this, what we consider a very material element in this, and that is that the oil business is just like ordinary manufacturing or ordinary other business, in that it will continue after the war, and that it will go on and help pay these taxes as long as high taxes remain caused by this war; so that it is not a fitting business that ought to be taxed heavily to-day on the theory that it will escape in the future. That is all I wish to say on that.

I wish also to call attention to the fact that, regardless of what you do in the way of taxation, we must go on producing. Our contracts call for production on the leases, in most instances, and regulations at the present time compel us to go on, practically, so that on proven territory we will go on, even if you take it all.

Senator GORE. Under a great many of those contracts, Judge, they can not stop, under penalty of forfeiture of the lease?

Mr. SHEA. Yes; and the department regulations compel it at the same time.

The price of oil is practically fixed by law. There is no way of raising the price of it. There is not, probably, any legal authority for that, but it is a regulation that comes from the Fuel Department of the Government under date of May 21, in which they stated that they would look with great disfavor on any attempt to raise the price of oil.

Senator DILLINGHAM. Above what?

Mr. SHEA. Above \$2.25 for Mid-Continent and \$1.85 for Texas and Gulf Coast.

Senator McCUMBER. How long ago was that?

Mr. SHEA. It was May 21.

Senator McCUMBER. Has not oil gone up and down since that time?

Mr. SHEA. No, sir; it has remained right there.

Senator GORE. This is crude oil, you know. Judge Shea speaks only for crude oil.

Mr. SHEA. I speak only for crude oil. Those that manufacture kerosene and gasoline and other things like that, I do not speak for them. They are purely factory matters, and their cost is pretty well defined; but with us the element of chance is very prominent.

One other thing I want to speak of: The definition of gasoline in the bill from the House is so vague and indefinite that many things not intended could be included, and with the definition it would be a tax very easily evaded. We will furnish you a printed definition of "gasoline," properly authenticated by the technical department of the Government in that matter that might aid in simplifying the matter and at the same time I think would be more just to every one. It would be extremely difficult to define gasoline. It means one thing in one place and another thing in another. For example, the gasoline that is being used in aeroplanes and in the high-powered engines of destroyers and the like of that, is an entirely different product from the gasoline you buy at a garage to fill the tank of your motor car; and the gentlemen connected with the business will appreciate a definition that will be more comprehensive than the one now in use, and better fitted to determine what it is.

Senator THOMAS. The difference is in the grade of refinement, is it not?

Mr. SHEA. Yes; there are different grades, and then there is blending afterwards. For instance, after the gasoline pays the tax it goes as gasoline where it is sold to the consumer, but before it is sold to the consumer it is again blended with kerosene and naphtha, and you do not get the product that is bought by the man who sells to you. That is constant and almost universal.

The things we will ask for I will briefly recapitulate. We believe that the oil business is a business of such a character that the war-profits tax ought not to be applied to it. We believe that it ought to be put under an excess-profits tax, and our view of it is that the present rate under the existing act is high enough.

Senator THOMAS. Are there many individual and partnership enterprises in your part of the country?

Mr. SHEA. Yes.

Senator THOMAS. Do you know why they should not be included in the war profits and excess-profits tax?

Mr. SHEA. No, sir; I do not know of any reason for the discrimination.

The second clause, we believe that to encourage this prospecting and exploration—or, as we call it in the oil business "wildcatting"—when a man discovers oil, until he gets his money back no tax should apply; that he ought to get that back before any tax is applied. Then he ought to be put on the same basis as other people.

Senator SMOOT. Do you think that same thing should apply to the mines in the West?

Mr. SHEA. I do not know why it should not, wherever the business is of this character.

Senator SMOOT. All mining is hazardous.

Mr. SHEA. To some extent; yes, sir.

Senator SMOOT. I think you have a more definite chance of getting oil, where a man will go and drill, than you have of getting ore.

Mr. SHEA. Well, that might be.

Senator GORE. Here is one trouble, Senator Smoot, that must be considered. Have you not known of instances where they would get fine producing wells, Judge, and 200 or 300 feet from them another man would get a dry hole?

Mr. SHEA. Yes. I have the experience of a gentleman who had that experience in another corner of an 80-acre lot.

Senator GORE. That is true of mineral mining, is it, also?

Senator SMOOT. Yes; I have known of instances where men have been within 25 feet and had nothing.

Mr. SHEA. That is not usual in oil.

Senator SMOOT. That is quite usual in mining for minerals.

Senator GORE. Do you have to make any such investment in mineral mining as has been made in these oil wells?

Senator SMOOT. Yes.

Senator GORE. Without being able to test it?

Senator SMOOT. Yes.

Mr. SHEA. I was answering the question. We believe that in mining for oil and gas we ought to let the discoverers get their money back that they have spent in exploration, and then begin to pay tax.

In case of sales, we believe that sales of newly discovered properties, found since 1918, the profit should have put on it a 20 per cent tax, to encourage sales and the changing of the property into hands that will produce more oil and bring it into the market of the country, and at the same time continue to pay tax.

The question of actual value of the property I have discussed pretty completely. We think that the money expended on the exploration and discovery ought to be treated as invested capital, to be returned by depletion.

The CHAIRMAN. Judge, there are gentlemen here, some of whom say they want to catch the 4 o'clock train.

Mr. SHEA. I am through this minute.

The CHAIRMAN. And I think they should be treated with some consideration.

Mr. SHEA. I do, too. I should like to ask that Judge Gill, of the Texas country, be given 5 minutes.

Senator THOMAS. Later on; there are others here now who must be heard.

The CHAIRMAN. We will have to give some of these other gentlemen an opportunity to be heard. Have you finished?

Mr. SHEA. Yes, sir.

Senator ROBINSON. Stick to your program, and then others may come in later.

Senator GORE. I would like to ask that Mr. E. D. Howard, nominee for Congress in the first district of Oklahoma, be allowed to file a statement in regard to zinc and oil, particularly showing its bearing on the taxation of the State.

Mr. SHEA. And we would like to have the privilege of filing an amended brief here.

The CHAIRMAN. You have that privilege. There are several gentlemen here who say they wish simply to make an appearance and file a brief. One of them is Mr. Taylor, representing the independent tobacco manufacturers of Winston-Salem, N. C.

(A statement was submitted by Mr. Shea, which is here printed in full, as follows:)

[Before the Finance Committee, United States Senate. Excess-profits tax and war-profits tax as applied to production of oil and gas, presented by Mid-Continent Oil & Gas Association and Texas Gulf Coast & Louisiana Oil & Gas Association.]

THE BUSINESS OF PRODUCING CRUDE OIL SHOULD NOT BE SUBJECTED TO A WAR-PROFITS TAX.

The production of crude oil is the most complete example of a wasting industry which has been called to our attention. The moment that oil is discovered it must be produced; it is fugitive in its character. The subdivisions of land from which it is produced are small; they are owned by many people, and unless each man produces to the capacity of his acreage his neighbor on the adjoining land will get his oil.

The storage of crude oil is a very expensive procedure, and loss from evaporation is very great. Therefore storage can only be carried on extensively by the very large companies. Individuals and moderate-sized companies, by the very nature of the business, are compelled to market their oil as produced.

From the sale of the first barrel of oil the producer is disposing of the corpus of his property, and is, in fact, marketing his capital assets; so that he must keep on reinvesting his money and finding new fields, making new discoveries, and producing oil from new sources in order to keep his business going.

The producer does not know whether he has an actual profit in the production of oil from any particular property until the entire investment in the same has been returned to him. The uncertainty of the amount of such total production always remains before him.

The discovery of oil rests very largely on chance or luck. There is no method other than actual drilling for discovering it, and, once it is found, the yield is problematical and in many cases very disappointing.

The hazard being so great, the reward should be, and in order to interest capital must be, in some degree commensurate with the risk.

Money can not be interested in producing oil with the same return from such investment as that from other enterprises, such as banking, manufacturing, and commerce.

IRREGULARITY OF RETURNS FROM OIL PRODUCTION.

The income from oil production is spasmodic and irregular. It depends originally so largely upon new discoveries and they are so uncertain and irregular that profits may be great in a year of low prices and small in a year of high prices for oil; so that in determining the profits accruing from the oil industry a series of years should be considered and the average profits for a period of years should be taken.

If the war-profits tax is to be applied, the net income subject to tax should certainly be the average for a period of years rather than for any single year.

NO WAR PROFITS IN THE PRODUCTION OF OIL.

We believe that there are no war profits in the production of crude oil. Labor and materials now cost on an average twice as much as they did in the prewar period. The production in the old fields has declined very rapidly and the wells that are being drilled in the mid-continent fields to-day have less than one-third the initial production that they had in the prewar period. The only new field now in sight is the Ranger (Tex.) field, in which oil is found at a depth of 3,400 feet, and in extremely difficult drilling, so that the production of oil from that field is bound to be very expensive and the development very slow.

In the case of each producer the necessary continued drilling results in failures and successes following each other in uncertain order, and a comparison of the income of one period with another—of the 1918 income with that of the prewar period—will disclose no profits due to the war, but merely that the oil producer has or has not, as the case may be, been more fortunate in finding oil in one period than in another. It may even occur that although the income for the taxable year is greatly in excess of the income for the prewar period,

nevertheless no profits have been made. This may be illustrated by the following example:

Corporation A, organized 1910.

Capital	\$100,000
Annual net income	25,000
Dividends paid to Jan. 1, 1918	200,000
Net income for 1918	50,000
War-profits tax	20,000
Per cent of tax to income	40
Total dividends paid	230,000

Corporation B, organized 1910.

Capital	\$100,000
Net loss to Jan. 1, 1918	80,000
Net income for 1918	50,000
Remaining deficit	30,000
War-profits tax	32,000
Per cent of tax to income	64
Deficit after paying tax	62,000

The price of Mid-continent oil and Texas and Gulf coast oil has been practically fixed by order of the Fuel Department. True, it is not a direct order, but the statement has been made by the fuel-oil department of the Government that it will look with disfavor on any attempt to increase the price of crude oil. Production is rapidly declining, and 2,400,000 barrels of oil were taken out of storage in the month of August, 1918.

EFFECT OF THE PROPOSED LAW.

The effect of the proposed law is to make it impossible for the small operator to go on prospecting for new properties. The large companies, with ample capitalization, can go on, because they can distribute their losses over the whole of the field in which they operate and apply them to the entire invested capital, and the result of losses to them will be to simply reduce profits, while the result of losses in explorations by individual operators and small corporations would mean financial disaster. The operator discovering and developing new properties and already possessed of an income that would put him in the war-profits class, would be compelled to give up 80 per cent of all his discoveries in the way of taxes to the Government and would find himself at the end of the war period in the position of having exhausted his property and having paid 80 per cent of the same in taxes to the Government—he would have neither property nor profit.

SALES OF PRODUCING PROPERTIES.

One of the characteristic and essential features of oil and gas producing is the individual or concern of small means engaged in prospecting. The flowing well is the rare exception and, as a rule, after the discovery of a producing property a large additional investment is necessary for development. It has been customary for the small operator to borrow through local banks this necessary money, both banker and operator knowing that the income from the property can not be expected to pay the loans when due, or even within a period proper and suitable for loans by banks of that type. In the past this has been possible because the operator has purposed selling the property when it had reached a suitable point of development, but treatment of all of the profits as income in the one year in which the sale is made and as subject to the existing excess-profits tax rates has stopped all sales of producing oil properties and is thus inevitably stopping prospecting by individuals and concerns of small means. The House bill with its increased rates under either alternative would greatly accentuate this unfortunate situation.

INVESTED CAPITAL.

In the case of the exchange of tangible property for stock under provisions of section 326 of the House bill, invested capital is defined:

"Actual cash value of tangible property other than cash bona fide paid in for stock or shares at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor."

It will be necessary in administering this law for the Treasury Department to ascertain the value of the tangible property paid in for stock in all cases.

It must ascertain this value for the purpose of determining whether the par value of the stock issued is in excess of the value of the property paid in, and in doing this it ascertains at the same time whether it is less than the par value of the stock issued therefor. In case the property paid in is of greater value than the stock issued for the same, upon what theory of equity and justice can the taxpayer be denied the value of such tangible property as invested capital when such value is allowed in case the par value of the stock issued therefor was equal to or greater than the value of such tangible property?

Article B, section 325, House bill, provides that the par value of stock or shares having no par value shall be deemed to be the fair market value of the same at the date of issue, and in a case where tangible property is exchanged for stock having no par value the fair market value would of course be the value of the property exchanged therefor, and in such cases full credit would be given for the value of such tangible property paid in for stock.

It is fair both to the corporation and to the Government that the actual value of tangible property paid in for stock regardless of the amount of stock issued therefor should be the measure of invested capital.

Large numbers of corporations have been formed merely as a matter of convenience, and as prior to the excess-profits tax law the question of invested capital did not enter into the amount or method of taxation these matters were not material.

The effect of this limitation would be to penalize the ultraconservative concern and put a possible premium on overcapitalization.

RAPID DECLINE OF PRODUCTION AND NECESSITY FOR PROSPECTING.

It is proper and necessary in the consideration of this legislation from any angle to keep in mind the fact that the production of all wells rapidly declines from the beginning. In the Midcontinent field the records show that the average well will produce from 35 to 50 per cent of recoverable oil during the first year of its life, and from 75 to 90 per cent during the first three years. In the Gulf coast field the decline is even more rapid and the life of the wells shorter. In the Goose Creek field in Texas, now very productive, the average life of a well does not exceed eight months, after which it must be worked over at great expense with much risk and problematical results.

It must be borne in mind also that to the Midcontinent field and the Gulf coast field—the latter composed of Louisiana and Texas—must the Government and the public largely look for maintenance of production by additional developments. The Ranger field of Texas is at present of inconsiderable production, but is a field of perhaps the largest promise. The oil is found at great depth in most difficult and expensive drilling and the method of drilling and development there has not yet been mastered.

CONCLUSIONS.

1. The principle or theory underlying the war-profits tax is inapplicable to the business of discovering and producing oil and gas, and we are, therefore, opposed to the alternative war profits and excess profits plan of the House bill. If the law as passed should retain this plan the income derived from the production of oil and gas should be excluded from the war-profits tax and be subjected to the excess-profits tax.

The rates of the existing excess-profits tax law are sufficiently high as applied to this industry and should be substituted for those of the House bill.

2. The deduction allowed should be in proportion to the cost of the capital, which, in the case of oil and gas producers, is not less than 15 per cent and is generally more, depending on the hazard of the particular venture. The new law should therefore provide for a minimum deduction of 15 per cent in the case of income from the production of oil and gas.

3. To encourage the prospecting vitally necessary to maintain the Nation's production, oil producers having discovered new deposits of petroleum unknown prior to January 1, 1918, should not be taxed on the income therefrom until all of the cost of discovering and developing such deposits has been returned.

4. In view of the importance and close relationship existing between sales of producing oil and gas properties and the continuance of the drilling in search of new production so vitally necessary to the prosecution of the war, the net

income derived from such sales, bona fide made, where not more than a 50 per cent interest is retained by the seller, should not be subjected to a greater tax than 20 per cent.

5. The actual value of tangible property other than cash bona fide paid in for stock or shares at the time of such payment should be the measure of invested capital.

6. Under existing law and the Regulations of the Treasury Department the cost of discovery of deposits of petroleum—that is, money spent in unsuccessful prospecting and drilling dry holes—must be treated as a loss, unless there is sufficient income during the taxable year to permit its deduction as an expense.

Obviously, this is a great and unjustifiable hardship and burden to the taxpayers engaged in such a hazardous and uncertain industry, the returns from which are so necessarily irregular that several years of losses frequently intervene between profitable discoveries.

Clearly, money so expended in such an industry should either be treated as capital invested and returnable through depletion or as an expense to be deducted from income when the same is attained in some subsequent year.

Inasmuch as the basic theory of our income-tax laws has been to forbid the carrying over of expense items from one taxable year to another, it is urged that the new law should provide that the cost of prospecting and development, other than the cost of physical property, in excess of income in any one year shall be added to capital returnable through depletion.

Respectfully submitted.

MID-CONTINENT OIL & GAS ASSOCIATION.

JOHN J. SHEA, *Chairman*.

J. R. COTTINGHAM,

E. B. HOWARD,

BARBETTE BLUE,

Committee.

TEXAS, GULF COAST, AND LOUISIANA

OIL & GAS ASSOCIATIONS.

By W. H. GILL.

The CHAIRMAN. Mr. W. B. Taylor, jr., desires to be heard now.

**STATEMENT OF MR. W. B. TAYLOR, JR., WINSTON-SALEM, N. C.,
REPRESENTING THE INDEPENDENT TOBACCO MANUFACTURERS
OF WINSTON-SALEM.**

Mr. TAYLOR. Mr. Chairman and gentlemen, I do not wish to make a speech, but I would like to have just about five minutes to read these few paragraphs which I have in typewriting here. There are only about four paragraphs.

Senator ROBINSON. Go ahead. You can get it done while you are talking about it.

The CHAIRMAN. If you will get through in five minutes, all right. I thought you simply wanted to present a brief.

(Mr. Taylor read the communication referred to, which is here printed in full, as follows:)

WINSTON-SALEM, N. C., September 12, 1918.

Hon. F. M. SIMMONS,

*Chairman Finance Committee,
United States Senate.*

DEAR MR. SIMMONS: We, the undersigned tobacco manufacturers of Winston-Salem, N. C., doing an approximate business of 7,000,000 pounds manufactured tobacco per annum, respectfully request that section 702, page 120, line 23, to page 121, line 9, of H. R. bill 12863 be changed, making the floor tax equal to one-half the difference between (a) the tax imposed by this act upon such articles according to the class in which they are placed by this title and (b) the tax imposed upon such articles by existing law other than section 403 of the revenue act of 1917.

First. The present styles and weights have been manufactured in good faith under the existing law and according to the statutory requirements.

Second. The object of section 702 appears to be to raise additional revenue quickly, but this would be defeated by creating a period of depression as it is obvious the dealer will not handle tobacco at a loss and the manufacturer should not be expected to show a loss on the stock he has manufactured and in process, which has been made by him in good faith. We further believe the proposed floor tax of 13 cents would be followed by a period of stagnation and loss of revenue to the Government.

Third. Present styles and weights are manufactured to retail at a fixed price, and the proposed increase of section 702, page 120, line 23, to page 121, line 9, would absorb more than the profit received by either the manufacturer or dealer.

Fourth. We respectfully ask that the dealer be taxed one-half of the proposed increase and that the manufacturer be given at least 30 days to dispose of his present stock and accommodate his styles and shapes to meet the new conditions.

Fifth. We feel warranted in making this request as to the floor tax and minimum of 30 days for manufacturers to change their styles by precedent established by Congress in previous legislation.

Respectfully submitted.

F. M. BOHANNON.
 BAILEY BROTHERS (INC.).
 BROWN & WILLIAMSON TOBACCO CO.,
 By R. L. WILLIAMSON.
 TAYLOR BROS.,
 By W. B. TAYLOR.
 J. G. FLYNT TOBACCO CO.,
 By T. P. FULTON.

JEWELRY.

The CHAIRMAN. The next gentleman is Mr. Meyer D. Rothschild. We will now hear him.

STATEMENT OF MR. MEYER D. ROTHSCHILD, NEW YORK CITY.

Mr. ROTHSCHILD. Mr. Chairman and gentlemen, I represent practically the entire jewelry industry of the United States. The jewelers' war revenue tax committee, of which I have the honor to be chairman, has some sixty-odd presidents of organizations, so that I may say I speak for the entire industry.

We come here to-day to say that we are entirely satisfied with section 906 of the proposed act, which imposes a tax of 10 per cent on all the articles handled by our industry when sold to the consumer.

We went before the Ways and Means Committee of the House and had a very extensive hearing, and upon the request of the Ways and Means Committee to present a 100 per cent proposition on our industry we presented such a proposition, taking in not only the articles which were taxed under the act of 1917, but all loose precious stones, silverware, watches, clocks, and kindred articles, with the result that we estimate the revenue under our proposed list of articles to be taxed will be from five to six and probably seven times the revenue to be derived under the act of 1917.

In other words, the Treasury Department estimated an income of \$7,500,000 from the jewelers. We estimate that if we are permitted to do such a normal business as we can do during the war we will turn in from forty to fifty millions of dollars of tax for the calendar year; possibly more.

We brought this matter to the attention of the House, and the luxury committee, of which Judge Hull is chairman, acquiesced in placing our tax on the jewelry when sold to the consumer, because,

obviously, the price of the goods when sold to the consumer is much higher than when sold by the manufacturer to the retailer. The Treasury Department found some fault with that classification because of the difficulty, as they saw it at that time, of administering the law where there are 35,000 jewelers involved as against four or five thousand manufacturers, importers, and producers. We had a conference, at which three members of the House were present, Mr. Roper and his assistants, the vice chairman and myself of the committee, and after a thorough consideration of the question the Treasury Department notified the Ways and Means Committee that they were convinced that the proposition we had made was a better one for the Treasury, and it could be administered, and that is the way the act stands at present; that is, 10 per cent when the goods are sold to the consumer, on all articles handled by the jeweler, which includes articles of great essentiality, which includes watches and clocks and some articles of silver-plated ware which ordinarily would not have been placed within the category.

In addition to that there is a section 907, and the following section, a paragraph of which provides for an additional tax of 10 per cent on all articles made partially or entirely of platinum. This is on page 135 of the bill. It reads as follows [reading]:

SEC. 907. That on and after November first, nineteen hundred and eighteen, in addition to the tax imposed by section nine hundred and six, there shall be levied, assessed, collected, and paid, a tax equivalent to ten per centum of the amount paid for any article commonly or commercially known as jewelry, composed in whole or in part of platinum, when sold for consumption or use.

Such tax shall be paid by the purchaser to the vendor and shall be collected, returned, and paid to the United States by such vendor in the same manner as provided in section five hundred and two. The vendor shall include in all returns made under this section the name and address of each purchaser, the price of each article sold to him and a description thereof, including the quantity and value of the platinum contained therein.

Platinum jewelry is provided for in section 906 among other jewelry, and it is probably almost the entire jewelry stock of the so-called better class of jewelers in the larger cities and forms a part of the stock of nearly every jeweler of any size in the country. It is provided for at 10 per cent, precisely as all other jewelry and watches.

Senator THOMAS. Is not that designed to discourage the use of platinum for jewelry?

Mr. ROTHSCHILD. Yes.

Senator THOMAS. Owing to the great demand for platinum in the arts and industries?

Mr. ROTHSCHILD. That is supposed to be the design, but that is precisely what I am coming to. It does not bring about that result. From the report of a hearing before the Ways and Means Committee, held on July 17 of this year, I am going to read a few lines.

Senator SMOOT. Will a tax of 20 per cent bring that about?

Mr. ROTHSCHILD. No, sir.

Senator SMOOT. Will 30 per cent?

Mr. ROTHSCHILD. The conservation of platinum?

Senator SMOOT. Yes.

Mr. ROTHSCHILD. No, sir; nothing will bring it about except the taking of the platinum by the United States Government, and the United States Government has said that it does not want it, that it will not buy it, and it has prepared and is about to issue licenses for the sale of that platinum jewelry.

Senator SMOOT. The Government of the United States has not enough platinum on hand now to fill the requirements that it will have before the end of this year for platinum. They have got to get it from some source.

Mr. ROTHSCHILD. The jewelers have offered, and, of course, are willing at any time the Government requires it, to give up this manufactured platinum and hand it over to the Government. The Government has declined to buy it; does not want it; will not take it. This is a revenue bill, as I understand it. There are millions of dollars worth of platinum in the hands of the retailers to-day.

Senator SMOOT. You mean in the shape of manufactured jewelry?

Mr. ROTHSCHILD. Manufactured jewelry; yes.

Senator SMOOT. But there are not millions of dollars worth of it in the shape of platinum itself.

Mr. ROTHSCHILD. That has all been commandeered by the Government. The jeweler can not make a single piece of platinum jewelry to-day. That is shut off absolutely.

Senator SMOOT. What the Government wants to do is to prohibit the manufacture of any more jewelry from platinum, if possible.

Mr. ROTHSCHILD. It has done that. The regulations are issued.

Senator THOMAS. That being so, how does this regulation hurt you?

Mr. ROTHSCHILD. I will get at that directly.

Senator THOMAS. All right.

Mr. ROTHSCHILD. Mr. Moore, in examining Mr. Summers, who is the Government official who has had charge of the platinum for the War Industries Board, at the hearing of the Ways and Means Committee which I have mentioned, asked him a number of questions, and I will read a few questions and answers from the printed record [reading]:

Mr. MOORE. Let me ask you this question, and then I am through: Do you think that the war exigencies of the Government are now such that it is necessary to prevent the jewelers of the country from selling such manufactured platinum as they may have in their possession?

Mr. SUMMERS. No. Emphatically no. The general policy of the War Industries Board is not to wreck an industry until it is absolutely necessary.

Mr. MOORE. In your judgment, the platinum agitation has been rather overdone?

Mr. SUMMERS. Overdone; positively overdone. * * *

Apart from the question of the necessity of the Government for platinum, which is admitted, the Government, through the officials who have been charged with this work of getting platinum, expressed itself repeatedly to the effect that it does not want the manufactured platinum—the jewelry of the jewelers. It will not buy it. They have said that they are perfectly willing that the jewelers should sell it. Now, under regulations that have been arranged between the War Industries Board and the Bureau of Mines there are about to be issued, I understand, on the 20th of this month, licenses to sell that jewelry. The jeweler is to be pledged when he sells platinum jewelry to keep a record, as is provided in this bill, of the name and address of the purchaser. He will receive a license from the War Industries Board to sell his platinum jewelry.

Senator SMOOT. The object of that is to know just where the platinum is.

Mr. ROTHSCHILD. Precisely.

Senator SMOOT. So that if exigencies do increase over and above what they are to-day, and it is necessary to get the platinum jewelry, they will know where to go and get it.

Mr. ROTHSCHILD. There is no objection to that. We are going to keep those records.

The bill, in paragraph 907, simply not only duplicates that and pledges the jeweler to send these records to the already overburdened Commissioner of Internal Revenue, but besides that—and this is the whole point, and it will afford just one more point upon which people who have been conducting a propaganda against the sale of platinum jewelry can hang some further arguments—if the United States wants the platinum which the jewelers have—the manufactured platinum—the United States can have it at any time. The United States, however, wants revenue. There are hundreds of millions of dollars' worth of gems, I believe, mounted in platinum, the platinum being but a small part of the piece of jewelry. Taking the liberty of taking a few things with me, I have brought here a few examples of this. There is a necklace that sells for \$12,000 [producing pearl necklace], and the platinum in that amounts to \$6. Under that act the jeweler that sells that piece will be obliged to pay \$1,200 additional as tax to cover \$6 worth of platinum.

Senator THOMAS. \$12,000?

Mr. ROTHSCHILD. \$12,000; \$1,200 to cover \$6 worth of platinum. There are a lot of instances of that kind. Here is a little cheap piece of jewelry of \$70 with the stones set in platinum [indicating]. The platinum amounts to 70 cents there.

Here is another which has the diamond set in platinum points. It is almost impossible to figure out what that platinum amounts to, and when you have figured it out you are taxing the platinum in that jewelry four or five hundred per cent, putting a burden on the jeweler that will affect his sales much more than if he were to make the sales and pay the tax.

Senator THOMAS. The value is not in the platinum, but it is in the value of the articles containing the platinum?

Mr. ROTHSCHILD. Yes; containing platinum. This is not conserving platinum, because if that were true, to conserve platinum, you would have failures from one end of the country to another. There are jewelers whose entire fortunes are tied up in platinum. It was an entirely legitimate business. They eventually gave up their platinum to the Government at \$105 an ounce, which was at a loss in some instances. It always cost them more than that, and in many instances it had cost \$120 an ounce, but as against other industries they gave up their platinum to the Government on a cost plus basis, and they are willing to give up to-day all the platinum they have and try to do something else with their gems, but the Government says: "We do not want your platinum jewelry; we are going to license you to sell the platinum jewelry. We do want this revenue, which in the case of platinum jewelry will amount to some millions of dollars." And at the same time a passage or paragraph is written in this bill which will have the effect of restricting the sale of platinum jewelry, and, as the author of this said: "It will leave the platinum in the hands of the jewelers. The Government does not want it."

What are we to do? It has not conserved any platinum. The platinum is here just as it was. It is in such a form that the Government can take it at any time it wants it. It is pure. The War Industries Board and the Bureau of Mines to-day, under a recent act passed, can take possession of the platinum, can control the use of platinum and the possession of platinum in everybody's hands—in the hands of the jeweler's or anybody's hands. The power is there. Now, these two organizations have come together and have made these rules and have prepared these licenses, and I shall file with the clerk, if you have no objection, a letter from Mr. Conner, of the War Industries Board, indicating in so many words just what the regulations are. If you will bear with me a moment, I will read you the regulations, which show you that the point is absolutely covered in the regulations which are about to be issued. This letter reads as follows [reading]:

WAR INDUSTRIES BOARD,
August 28, 1918.

From: Platinum section.

To: Hon. Claude Kitchin, chairman Ways and Means Committee, Washington, D. C.

Subject: Rules and regulations pertaining to the licensing of use of platinum, iridium, and palladium.

1. I am handing you herewith paragraphs relating to the use of platinum by the manufacturers of platinum jewelry and the keeping of records pertaining thereto.

2. These paragraphs are in connection with the regulations promulgated under the provision of the act of October 6, 1917, as amended by the act of July 1, 1918, authorizing the Director of the Bureau of Mines, under rules and regulations approved by the Secretary of the Interior, to limit, during the period of the war, the sale, possession, and use of platinum, iridium, and palladium and compounds thereof.

3. The rules and regulations were drawn up by a joint committee of the War Industries Board and the Bureau of Mines, and the administration of the licensing of the use of platinum will be conducted by this section of the War Industries Board.

4. I would respectfully request that these paragraphs from the rules and regulations be kept confidential, as plans are not yet prepared for the publication of same.

C. H. CONNER,
Chief Platinum Section.

11. From and after the date of these regulations, under the penalties prescribed by section 19 of the act of October 6, 1917, no person * * * shall:

(a) Use any platinum or platinum scrap, iridium or iridium scrap, palladium or palladium scrap, and (or) compounds thereof, in the manufacture, alteration, or repair of any ornament or article of jewelry.

If that was strictly construed, then a man selling a ring for \$10,000 which is too small for the purchaser may not enlarge that ring by the addition of a few grains of platinum without a special permit, and under this arrangement it does not indicate that permission will be given [continuing reading letter]:

All licenses shall be issued in the name of the Director of the Bureau of Mines and countersigned and delivered by the War Industries Board, and shall be and remain subject to the following conditions:

(c) Records shall be kept by each licensee of all his sales, purchases, and other transfers of platinum, iridium, or palladium, or compounds thereof, and of articles containing platinum, iridium, or palladium, or compounds thereof, with the names and addresses of the purchasers, sellers, and (or) transferees, and the quantities involved, which records shall be open at all reasonable times to the duly authorized representatives of the Director of the Bureau of Mines.

This is an official letter, dated August 28, 1918, from the War Industries Board. I will file that letter.

The CHAIRMAN. The effect of that would be that hereafter as long as that remains in force no platinum will be used in the manufacture of jewelry?

Mr. ROTHSCHILD. Yes; absolutely.

Senator SMOOT. All your troubles will be over in a little while. We passed a bill in the Senate day before yesterday authorizing the Government to go into the mining business for platinum, and they are going to send out a lot of high-school graduates, and we will have more platinum than we will know what to do with in a little while.

Mr. ROTHSCHILD. I believe there is a shortage of platinum, and if this were a conservative measure I would not oppose it, if it really were a conservative measure. It is nothing but an irritating measure which, if it succeeds in the intent of its authors, may interfere with the sale of platinum jewelry which the Government does not want and will not take. I submit that is an intolerable situation.

The CHAIRMAN. You would not care anything about this 10 per cent tax if it applied only to jewelry hereafter manufactured with platinum in it?

Mr. ROTHSCHILD. Not the slightest objection to that; it would be superfluous, because I assume that the Government will enforce that order and can enforce it.

The CHAIRMAN. It would apply only to jewelry hereafter manufactured. It would be only supplementary to that, if that is effective, and the other would not hurt you?

Mr. ROTHSCHILD. Not at all, sir.

The CHAIRMAN. Now, suppose this tax were so made and revised as to apply only to future manufactures. Then, you say that it is a very unjust tax that applies to the jewelry already manufactured containing platinum, in that it taxes not only the platinum in the article but taxes the value of the completed article?

Mr. ROTHSCHILD. Yes; from two or three times to twenty times as much as the value of the platinum; sometimes one hundred times as much.

The CHAIRMAN. Suppose, then the tax on the jewelry already manufactured were confined to the platinum contained in that jewelry?

Mr. ROTHSCHILD. It would be a small item. It would not help the Government. I heard of one concern that has a stock of \$2,000,000 worth of jewels set in platinum in which the value of the platinum is \$18,000. It would be very difficult to determine in a practical way what the platinum value is, and the amount yielded to the Government would be so small that it would simply be irritating and very difficult of administering.

The CHAIRMAN. You could have ascertained, approximately, the platinum value?

Mr. ROTHSCHILD. Yes; but it would be very objectionable.

The CHAIRMAN. Your point is that then it would not raise any revenue?

Mr. ROTHSCHILD. It would not raise any revenue at all, and it might interfere somewhat with the sale of the jewelry.

The CHAIRMAN. You have no objection to this tax if it applied only to jewelry hereafter manufactured?

Mr. ROTHSCHILD. Not the slightest. I see no reason for it, but I see no objection to it.

Senator SMOOT. No reason for it?

Mr. ROTHSCHILD. We came up a year ago and said that we were willing to pay the tax. We have lived up to that. We showed the Department of Internal Revenue loopholes in the bill. We threw into the bill all the unmounted stones, and things that were not covered, by asking for and getting a ruling from the Treasury Department to the effect that loose goods, when sold to the consumer, were subject to that tax. This probably doubled the amount of revenue to the Government. Now, we have gone to the House, and in answer to the request we have estimated our business in normal times to be from five hundred to six hundred million dollars, not only jewels but watches, clocks, and such things as jewelers sell, and which by jewelers are sold at all the way from 50 to 100 per cent higher than when they leave the manufacturing jeweler's hands, on account of the heavy overhead. That will mean forty or fifty million dollars to the Government.

If this proposed platinum tax in section 907 were really a revenue producer, we would not feel like coming to you and objecting. It is not only not a revenue producer but, if persisted in, there will be less revenue than if you leave that under the 10 per cent provision of 1906; and if it does succeed in very greatly cutting down the sale of platinum jewelry, it will mean distress throughout the country on the part of men who ought not to be punished for simply going on and making up these jewels with platinum when they had a perfect right to make them up, investing their fortunes in them, paying a heavy duty on the jewels, and then finding themselves facing the situation where the Government says, "We do not want your jewelry. Go ahead and sell it. We want the revenue, and we are giving you a license to sell the jewelry." That is the situation, gentlemen, and I hope that the Senate will amend this bill by striking out section 907.

I would like to file with the committee a brief memorandum, and a little later I will go into the thing more thoroughly.

Senator ROBINSON. You mean that you want to file another statement?

Mr. ROTHSCHILD. I would like to file another statement later.

Senator ROBINSON. Yes.

Mr. ROTHSCHILD. That is all. Thank you.

(A memorandum was submitted by Mr. Rothschild, and is here printed in full, as follows:)

"SEC. 907. That on and after November 1, 1918, in addition to the tax imposed by section 906, there shall be levied, assessed, collected, and paid a tax equivalent to 10 per cent of the amount paid for any article commonly or commercially known as jewelry composed in whole or in part of platinum, when sold for consumption or use.

"Such tax shall be paid by the purchaser to the vendor and shall be collected, returned, and paid to the United States by such vendor in the same manner as provided in section 502. The vendor shall include in all returns made under this section the name and address of each purchaser, the price of each article sold to him, and a description thereof, including the quantity and value of the platinum contained therein."

First. This additional jewelry section was admittedly placed in the bill with the intention of discouraging the further use of platinum metals for the manufacture of jewelry.

Second. It is also intended to procure a record for the Government of all private purchases of platinum jewelry in order that the Government may have the names and addresses of such purchasers and the amount of platinum contained in the jewelry purchased in case the Government should at any future time desire to acquire this platinum.

Third. The War Industries Board and the Bureau of Mines now have the absolute power to control the possession and use of all platinum metals and have recently come to a joint agreement for the regulation of such possession and use.

Fourth. These regulations, signed by the proper officials, are now being printed and will be issued about September 20. They prohibit all further use of the platinum metals in the manufacture of jewelry and provide a complete system for licensing the purchase and sale of the platinum jewelry now manufactured composed wholly or in part of such metals.

Fifth. These regulations require a complete record of sales to private purchasers identical with the second paragraph of section 907, which should therefore be eliminated from the bill.

The Government, through the War Industries Board and Bureau of Mines, already has the power to commandeer platinum jewelry in the hands of manufacturers, retailers, and even private owners. Section 907 of the bill is therefore superfluous.

Sixth. In the course of an extensive hearing, held on July 17, 1918, on the entire platinum question before the Committee on Ways and Means the Government official responsible for the purchase and conservation of platinum gave the following answers to questions put by Congressman Moore:

"Mr. MOORE. Let me ask you this question, and then I am through: Do you think that the war exigencies of the Government are now such that it is necessary to prevent the jewelers of the country from selling such manufactured platinum as they may have in their possession?"

"Mr. SUMMERS. No; emphatically no. The general policy of the War Industries Board is not to wreck an industry until it is absolutely necessary.

"Mr. MOORE. In your judgment, the platinum agitation has been rather overdone?"

"Mr. SUMMERS. Overdone; positively overdone * * *."

The Government officials responsible for the handling of platinum have repeatedly stated that the Government did not wish to buy manufactured platinum jewelry and had no objection whatever to the jewelers selling such jewelry in the regular course of their business, and they are, as before stated, about to issue licensing regulations authorizing jewelers to sell such finished platinum jewelry.

Many millions of dollars are invested in platinum jewelry, the greater part of the value, however, being in the gems, and the smaller part, of course, being in the metal.

The sale of platinum jewelry will, at the 10 per cent rate of taxation imposed on all jewelry, provided for in section 906 of the bill, produce a very substantial revenue to the Government, as many stocks of the more important jewelers in the large cities are composed almost entirely of this class of merchandise. Any effort to discriminate against this particular variety of jewelry will be seized upon by the propagandists, who have been stating that the purchase of platinum jewelry is unpatriotic, and the result will undoubtedly be twofold:

In the first place, it will undoubtedly restrict the sale of such jewelry, with the result that many men who have their entire fortune invested in platinum jewelry and the gems mounted therein will be seriously crippled, and if the propagandists are really successful many will be forced into bankruptcy.

In the second place, such a falling off in sales will seriously reduce the revenue which the Government needs and would otherwise receive from such sales.

The second paragraph of section 907 simply duplicates the work of the jeweler in compelling him to furnish information to the Department of Internal Revenue which he will be required by the regulations of the War Industries Board and the Bureau of Mines to keep for their inspection. This will not only throw additional work on the jeweler, but unnecessary work on the Department of Internal Revenue.

JEWELERS' WAR REVENUE TAX COMMITTEE,
MEYER D. ROTHSCHILD, *Chairman*,
6 West Forty-eighth Street.

(The following statement was subsequently submitted by Mr. Rothschild, and is here printed in full, as follows:)

STATEMENT OF JEWELERS' WAR-REVENUE TAX COMMITTEE.

ATTITUDE OF THE JEWELERS TOWARD THE WAR EXCISE TAX OF 1917.

On May 12, 1917, a committee representing the jewelry trade of the United States appeared before the Senate Finance Committee and expressed the willingness of the jewelers of the country to bear any just share of the war burdens which Congress might impose.

Acting in this spirit, the jewelers' war revenue tax committee, after the act became a law, offered its services to the Treasury Department to assist in working out the technical details of the commodities tax as applied to jewelry.

It soon developed that, under the restrictions of the former Treasury decisions and definitions, unset precious stones and pearls and imitations thereof and watches of all kinds could not be taxed under the act. The jewelers, however, held meetings to consider the situation, and, actuated by the desire to do their share to help win the war, directed the jewelers war-revenue tax committee to recommend to the Treasury Department that certain classes of watches be considered jewelry for the purposes of the war excise act and that all unset precious stones and pearls and imitations thereof and all parts of jewelry be considered as covered by the act when sold to the consumer. Treasury decisions were rendered in accord with this voluntary submission of these extra articles to taxation, and we are happy to state that no jeweler has ever objected to these decisions, although our trade is well aware that they could have been legally questioned. In this manner the jewelers helped to carry out what was probably the intent of Congress, and, notwithstanding mistaken views to the contrary, we have no hesitation in stating that every piece of jewelry sold by the manufacturer, producer, or importer after October 3, 1917, was subject to the sales tax of 3 per cent, and all unset gems were taxed as soon as they were set and sold or if sold to the consumer in an unset condition, thus preventing any loss to the Treasury because of omission to tax this important part of the jeweler's stock.

For further details as to the manner in which the jewelers war revenue tax committee cooperated with the Treasury Department we respectfully refer you to the Commissioner of Internal Revenue.

THE NEW REVENUE BILL.

As soon as the consideration of the new revenue bill was announced, a mass meeting of the entire jewelry trade was called for June 6, 1918. A large number of manufacturers, importers, wholesalers, and retailers met at the rooms of the Merchants' Association in New York City and, after authorizing the appointment of a representative war-revenue tax committee, passed the following resolutions:

"Whereas the President has urgently requested Congress to provide additional revenue from incomes, excess profits, and luxuries; and

"Whereas the jewelers of the United States are willing, as they have been in the past, to do their full share in helping win the war: Be it

"Resolved, That the jewelers of the United States, in mass meeting assembled, instruct their war-revenue tax committee to cheerfully acquiesce in any and all fair, equitable, and uniform taxes which may be laid upon the sale of our commodities; and be it further

"Resolved, That as it is our earnest conviction that the maximum amount which can be expected from a sales tax on luxuries and so-called semiluxuries will be entirely inadequate to meet the requirements of the situation, the jewelers war-revenue tax committee be, and is hereby, instructed to present to the Ways and Means Committee of the House of Representatives and to the Finance Committee of the Senate the request that serious consideration be given to a small uniform sales tax on each and every sale or transaction involving the transfer of any and all varieties of goods, wares, and merchandise."

These resolutions were approved at the convention of the New York State Retail Jewelers' Association, who recommended that the tax should accrue on the sale to the consumer, and we find this to be the opinion of all the retail jewelers we have been able to reach.

A committee was appointed consisting of the presidents of practically every jewelry and kindred organization in the United States, and a special subcommittee was selected to appear before the Committee on Ways and Means in Washington on July 10, 1918. It developed during this hearing that the Committee on Ways and Means was desirous of taxing a number of articles sold by jewelers which have hitherto not been taxed, and a request was made of the jewelers war-revenue tax committee for a list of such articles and for suggestions as to the form of section to cover our commodities in the new revenue act.

After our hearing before the Committee on Ways and Means a special committee of retail jewelers was appointed with instructions to submit such a new list of taxable articles and the text for a new jewelry section. This committee made its report to the full committee on July 19, 1918, and after thorough discussion its recommendations were unanimously adopted. We submit that report herewith as the recommendation of the jewelers' war-revenue tax committee. The per cent of taxation by Congress is left blank, but we wish to say that the committee stated that in its opinion a 5 per cent tax levied, as it suggests, on the articles covered by this proposed section of the new war-revenue tax law will return at least six times the revenue which the present act produces at 3 per cent tax levied on our present schedule when sold by the manufacturer, producer, or importer.

The list of articles covered by the present section and by the proposed new section is marked "Exhibit A," and is printed at the end of this statement.

EXACT COPY OF PARAGRAPH REFERRING TO JEWELERS' TAX, WAR-REVENUE TAX ACT, PASSED OCTOBER 3, 1917.

SEC. 600. That there shall be levied, assessed, collected, and paid: (e). Upon any article commonly or commercially known as jewelry, whether real or imitation, sold by the manufacturer, producer, or importer thereof, a tax equivalent to three per centum of the price for which so sold.

PROPOSED PARAGRAPH TO BE SUBSTITUTED FOR SECTION 600 (e), WAR-REVENUE TAX ACT, PASSED OCTOBER 3, 1917.

That there shall be levied, assessed, collected, and paid: Upon any article commonly or commercially known as jewelry, whether real or imitation; pearls, precious and semiprecious stones and imitations thereof; articles of adornment or utility when made of or ornamented with precious metals or imitations thereof; ivory articles; watches; clocks; bronze and marble statuary and imitations thereof; umbrellas, canes, and crops when mounted with precious metals; leather goods, silk and other similar materials when mounted with precious metals or when fitted with precious metals, imitations thereof, or ivory; opera glasses, marine glasses, field glasses, and binoculars, when sold to the consumer, a tax equivalent to — per centum of the price for which so sold.

NOTE.—Certain jewelry stores sell stationery, china, glass, cutlery, fans, furniture, lamps, pottery, and bric-a-brac.

Without the establishment of a price limit as a basis for taxation, which has proven most unsatisfactory where tried, your committee suggests that the Ways and Means Committee place these articles under their proper classifications, namely: Glass, china, bric-a-brac, lamps, furniture and cutlery under house furnishings; stationery under the commercial stationer or paper trade, etc.

We beg leave to lay great stress on two points in connection with the foregoing recommendation:

1. That in order to do the maximum of business under war conditions and therefore to make the greatest monetary return to the Treasury, it is important that all the merchandise sold by the jeweler and included in the foregoing schedules—luxuries, semiluxuries, articles of utility, and articles of prime necessity—be grouped together under the same rate of taxation. To indicate by the tax rate that some part of a jeweler's stock of merchandise is singled out for higher taxation would seriously affect his entire sales and so reduce the revenue. There are naturally adverse war conditions for many jewelers and, except in communities where exceptionally high wages may stimulate the purchases of the jewelers' wares, it will be necessary for many of the 30,000 retail jewelers to make great efforts to sell the stocks of merchandise they have on hand in order to meet their obligations and earn a living.

If any of the goods sold by jewelers are placed in a separate class, public attention will be directed to such segregation with the probable result that

many people may consider it unpatriotic to buy from jewelers. A large falling off in sales may mean widespread bankruptcy, not only of the retail jeweler, but of the wholesaler who is his creditor.

Any considerable disturbance of this kind must affect the banks, and the Treasury will thus be doubly hit; it will lose revenue, and the Federal reserve banks may be obliged to repair some of the damage.

2. The jewelers' war-revenue tax committee strongly urges upon the Committee on Ways and Means the justice and fairness of taxing us with, and at the same rate as, automobiles, musical instruments, sporting goods, and cameras, with which we are now classified in Article VI, war excise taxes, section 600 of the act of October 3, 1917, and that as many more similar commodities as possible be added to this group in the interest of fair play and of an increased revenue.

If we are retained in this group, or an enlarged group, jewelers are ready and willing to pay any fair, just, and reasonable tax, provided, however, that the same per cent of tax is placed on every other member of the group.

TAX YIELD.

The tax based on the sale of goods by the retail jeweler to the consumer will yield a very much greater revenue than when based on the sale by the manufacturer, producer, or importer.

First. The selling price of the retailer will, because of intermediate profits, expenses, and his own gross profit, average 50 per cent higher than the price of the manufacturer, producer, or importer; hence the return to the Treasury will be 50 per cent greater.

Second. Retailers have stocks of merchandise which are not now subject to the sales tax under the act of 1917, but which would be subject to the new sales tax when sold to the consumer under our proposed section of the new act.

Third. Goods manufactured, produced, or imported since October 3, 1917, and still in the hands of the retailer when the proposed new act becomes a law will have paid a sales tax to the Treasury of 3 per cent, and the 5 per cent we suggest will be an additional sales tax on such merchandise.

Apart from the fact that because of war conditions there will be a restricted output of many commodities handled by jewelers, which would make a tax on the manufacturer, producer, or importer a diminishing one, we have shown that a very much larger amount of revenue can be collected by the levy on goods when sold to the consumer.

TAX LIMIT.

While we suggest a 5 per cent sales tax to be levied in the manner above indicated, we are prepared to pay a higher tax, if Congress decides that it is necessary to put a heavier burden on the commodities with which we are now grouped.

After canvassing all branches of our trade, we are of the opinion that we could pay any sales tax when goods are sold to the consumer up to 10 per cent without disastrous results to our business, provided, however, that the like per cent of tax was placed on the other commodities with which we have been grouped.

PASSING TAX TO THE CONSUMER.

In order to restrict sales as little as possible, the retail jeweler must probably embody the sales tax in the selling price of his commodities. This will benefit the Treasury from two angles: First. It will insure the maximum of sales by the retailer. Second. As the amount of the sales tax will be included in the selling price of the commodity, the Government will collect a tax on the tax so included, which will aggregate a considerable sum. For the reasons above stated, and because jewelers seldom give invoices for goods sold over the counter, the suggestion that the tax be collected by affixing revenue stamps to bills or sales slips is not a workable one, and we therefore do not approve of the use of revenue stamps in connection with our commodities.

JEWELERS' SALES.

In making a very rough estimate of jewelers' sales to consumers, covering their entire sales, we have established the following tentative figures: Whole number of retail jewelers, 30,250. Of these, 15,000, or 50 per cent, average

\$1,000 of sales each per annum; 12,000, or 40 per cent, average \$27,500 of sales each per annum; 3,000, or 10 per cent, average \$82,000 of sales each per annum.

The remaining 250 are the larger retail jewelers of the country, whose sales will probably run from \$100,000 to \$1,000,000 or over per annum.

The group of 30,250 retail dealers referred to is listed by the National Jewelers' Board of Trade and consists not only of jewelers, but includes others who have jewelry departments, etc.

It has been variously estimated that the articles covered by our proposed new tax section will, in normal times, show sales by the 30,250 retail dealers of from five to six hundred million dollars (\$500,000,000 to \$600,000,000). In addition, there are many other dealers who sell articles included in our proposed new tax section, but we have no data upon which we could form an estimate of the total of such sales.

While this indicates that 15,000, or 50 per cent, of the retail jewelers sell only about 10 per cent of all the merchandise, these smaller merchants are very important to the country by reason of the fact that they are the watchmakers and repairers upon whom their communities depend entirely for a highly essential, indispensable service. None of these jewelers could pay their expenses and make a living solely from watch repairing. They must, therefore, depend largely upon their sales of merchandise. Any action by Congress which will seem to make the purchase of jewelry unpatriotic will bear most heavily on this half of a great industry. The small jeweler must sell his goods to pay his debts and support his family. His more successful brother jeweler may have some reserve to tide him over the period of the war, but a prohibitive tax, or a tax discriminating against jewelry as unpatriotic, would probably result in ruining many of this class also.

ANY TAX WHICH WILL PREVENT THE RETAIL DISTRIBUTOR FROM DOING A PROFITABLE BUSINESS WILL ADVERSELY AFFECT THE AMERICAN MANUFACTURER OR PRODUCER.

Jewelry manufacturers are curtailing their output for a number of reasons. Many of their men have been called to the colors or have left the industry and taken more lucrative jobs. Because of comprehensive commandeering of platinum metals by the Government and the complete control in the use of those metals now lodged in the Bureau of Mines, it is safe to say that platinum jewelry can no longer be manufactured. Some jewelry manufacturers are already engaged in making war materials, and many more have recently responded to a Government request for surgical instruments and are trying to make these much needed articles.

The jewelry manufacturer is therefore facing the difficult problem of trying to keep some kind of an organization together, in order that he may be in a position to get into his old stride again when the war ends.

England and France are preparing for export trade after the war, and the jewelry business of Cuba, Central, and South America is a prize for which those countries will strive in competition with Germany and the United States.

A special agent of our Department of Commerce has recently been in Cuba and is now traveling through South America in the interest of our jewelry export trade. He wrote early this year:

"Our bureau is trying to do a permanent service for the jewelry industry by helping it to take full advantage of the opportunities which exist in Latin America. This service, we hope, will be a benefit to the trade long after the war has ceased and not merely for the duration of the war."

American jewelry, like other American wares, is a part of our country's commerce, and it is unthinkable that Congress will do anything to unnecessarily injure this great industry.

SMALL UNIFORM SALES TAX.

The resolution hereinbefore quoted asks Congress to give serious consideration to a small uniform sales tax on each and every sale or transaction involving the transfer of all varieties of goods, wares, and merchandise.

We believe this to be an economically sound method of taxation. As the needs of the Government increase, the percentage can be raised; as they decrease, the tax can gradually be decreased to the vanishing point.

We are assured by those who have made a study of this method of taxation that a very large revenue can be collected without the slightest injury to commerce.

Up to this time we have not laid great emphasis upon this feature of our resolution, as we did not wish it to appear as though we were trying to shift the burden of the tax. We disclaim any such intention, because the only purpose of our suggestion is to secure a maximum revenue through a small tax, widely distributed.

If Congress thinks it wise, however, to restrict the commodities tax to comparatively few articles and to make the rate correspondingly high on those few articles, we have no further objection to offer.

Where there may be a popular demand at this time for a tax on luxuries, semiluxuries, and so-called nonessentials, the controlling aspect of the situation is the solution of the problem of revenue from the new tax act, and we seriously doubt if a reasonable tax on a limited number of commodities will result in any such vast return to the Government as a small tax on the sale of all goods.

RESTRICTING THE PRODUCTION OF LUXURIES, SEMILUXURIES, AND OTHER NONESSENTIAL ARTICLES THROUGH EXCESSIVE TAXATION.

Much has been spoken and written as to the prime necessity of releasing men and material and conserving fuel, freight, and cargo space by restricting the production of so-called nonessentials during the period of the war.

We concede that the Government, through its Executive, should take every man and every bit of material which may be required to help win the war; but when an industry has yielded up such men and materials from time to time as the needs of the war require, every assistance compatible with our war program should be given such industry to keep it alive for those after-war days, when industries which may now properly be deemed nonessential will become essential to the well-being of the Nation.

It is a fact that the majority of the people of this country are engaged in industries which are not directly contributing to the prosecution of the war, but they are none the less indispensable to the success of this country in its struggle for victory. While many of these people are small dealers, manufacturers, or distributors of merchandise, they make up the great bulk of the mercantile class of the United States. Any suggestion that nonessential industries, or even luxuries or so-called semiluxuries, can be safely taxed out of existence during the period of the war will have to reckon with the concrete suggestion that this would spell bankruptcy, not only for hundreds of thousands of people, but would materially increase the burdens of our Government in forcing it to take care of the families of soldiers who are now serving the country.

Jewelers make no special claim to patriotism, but they have no hesitation in pointing to their record during the past year as an indication of the manner in which our industry has met the requirements of the Government in the way of a special commodities tax. We have no complaint to make that the manufacture of platinum jewelry has been absolutely stopped through Government action. If the further requirements of the Government for the war necessitate the taking of manufactured platinum in the hands of jewelers, we are on record as stating that we will cheerfully accept the situation when it arises. We understand that the Government officials who have intimate knowledge both of the requirements of the Government for the platinum metals for war purposes, and of the stocks of metal available to the Government on hand in this country, have officially stated to the Committee on Ways and Means that the Government has sufficient platinum on hand for its needs and that the stocks of manufactured platinum in the hands of jewelers are not required. We repeat, however, that if at any time these stocks are required for the Government they will be forthcoming.

IN CONCLUSION.

At our hearing before your committee one of your members requested us to make a 100 per cent proposition to Congress. We beg to state that our proposed section for the new revenue act covers all our commodities, many of which are articles of necessity and utility, and is in every way the 100 per cent proposition asked for.

Respectfully submitted.

**JEWELERS' WAR REVENUE TAX COMMITTEE,
MEYER D. ROTHSCHILD, Chairman.**

JULY 23, 1918.

The CHAIRMAN. We can hear from you now, Mr. Dunham.

STATEMENT OF MR. JOHN H. DUNHAM.

Mr. DUNHAM. I would like to call your attention to section 906, page 134, of the bill. Under this clause "all articles commonly and commercially known as jewelry whether real or imitation."

Senator THOMAS. We have heard from two gentlemen already upon that section.

Mr. DUNHAM. I only want to speak in regard to watches and clocks in their classification of jewelry. We have taken that matter up with the War Industries Board, as to the status of alarm clocks and nickel watches. They have decided, after an investigation that they have made, that those two items are necessary to industry—that is, that the workman depends upon the alarm clock to get him up in the morning, and that it is only bought for the purpose of industrial use, and for that reason they have decided that it is a necessary thing. It seems to us not exactly the intent of the Government to class a necessary article with such articles as jewelry.

The same thing is true of nickel watches.

Most alarm clocks are sold anywhere from \$1.25 to \$3.50 each. Nickel watches are sold in normal times for \$1 to \$2. In these times they are sold at from \$1.50 to \$2.50.

Those articles are principally bought—probably 90 per cent or more—by workmen, and it seems to us that they should come under some classification of necessities. If you are taxing all necessities, then there is nothing to be said whatever about it; but we think that they could not be classed as jewelry; they should be given some classification, as in section 905, where you gave a minimum war use of so much for a watch and a minimum price for clocks; that would cover the matter completely. It is purely a question of whether they are a luxury or a necessity. Thank you.

The CHAIRMAN. The committee will now hear Mr. F. C. Nichols.

STATEMENT OF MR. F. C. NICHOLS, VICE PRESIDENT OF COLT'S PATENT FIREARMS MANUFACTURING CO., HARTFORD, CONN.

Mr. NICHOLS. I am vice president of Colt's Patent Firearms Co, of Hartford, Conn. I also represent the Savage Arms Co., of Utica, N. Y.; the Smith & Wesson Co., of Springfield, Mass.; the Harrington & Richardson Arms Co., and the Worcester Arms Co., and the Iver Johnson Arms & Cycle Works, of Fitchburg, Mass.

I will only take up a moment of your time. I want to refer to title 9, section 900, paragraph 11 of the bill, which imposes a tax of 25 per cent on all revolvers and pistols sold by the manufacturer (other than such as may be sold during the present war to the United States, political subsidiaries thereof, or allied nations), as against a tax of 10 per cent on rifles, shotguns, shells, and cartridges. We submit that this constitutes a most unfair and unwise discrimination as against the manufacturers of pistols and revolvers; that the manufacturers of pistols and revolvers should be taxed as much, and only as much, as the manufacturers of shotguns and rifles.

I need not remind you gentlemen of what the manufacturers of small arms have done to help win this war, and it seems hardly fair to us that such a tax should be placed, which would materially affect our income and our business in times of peace.

Senator THOMAS. What would you think of such a tax upon the owner of firearms? Of course, you are aware that a great many firearms are carried concealed, and that that causes many offenses in the country. It has occurred to me that the owner of firearms might not only prove a source of revenue, but that might diminish that very dangerous practice.

Mr. NICHOLS. Of course, this tax of 25 per cent will have to be borne by the purchaser.

Senator THOMAS. I am talking now about a substitute for this, by placing a tax on the owner of the weapon. In other words, if a man totes a gun in his pocket, to use a western expression, why should he not pay a tax upon it?

Mr. NICHOLS. A tax of 25 per cent would affect the sale of the firearm. A tax of 25 per cent or of 2,500 per cent would have no deterring effect upon the crook or the man who wanted to possess a firearm for such a motive.

Senator PENROSE. Has not the sale of pistols to the individual fallen off to a negligible quantity in the last year or so?

Mr. NICHOLS. No, sir.

Senator PENROSE. Has not the State of New York passed a law forbidding the sale of revolvers, or regulating it?

Mr. NICHOLS. It regulates it to the extent that a man must have a State or a city license to carry before he can purchase. It has affected somewhat the sale of small arms in New York State.

Senator PENROSE. I incidentally happen to know that in the eastern part of the State of Pennsylvania and in Philadelphia it is very hard to buy a revolver.

Mr. NICHOLS. Is that recently?

Senator PENROSE. Recently; yes.

Mr. NICHOLS. The manufacturers are not producing any small arms for the general market since the war began.

We have covered these matters quite extensively in our argument, which I would like to file with the committee.

Senator SMOOR. You would be satisfied with the same percentage of tax on your firearms and cartridges that is provided in paragraph 11 of that section as is imposed upon shotguns and rifles?

Mr. NICHOLS. Yes, Senator.

(A memorandum was filed by Mr. Nichols and is here printed in full, as follows:)

MEMORANDUM FOR MANUFACTURERS OF PISTOLS AND REVOLVERS.

The proposed revenue bill (Title IX, sec. 900, par. 11) imposes a tax of 25 per cent on all pistols and revolvers sold by the manufacturer (other than such as may be sold during the present war to the United States, political subdivisions thereof, or allied nations), as against a tax of 10 per cent on rifles, shotguns, shells, and cartridges.

We submit that this constitutes a most unfair and unwise discrimination as against the manufacturers of pistols and revolvers; that the manufacturers of pistols and revolvers should be taxed as much, and only as much, as the manufacturers of shotguns and rifles.

THE PROPOSED DISCRIMINATORY TAX WILL PRODUCE NO MATERIAL REVENUE DURING THE WAR, AND, THEREFORE, SHOULD NOT BE INCORPORATED IN A GENERAL REVENUE BILL.

There are practically only five manufacturers of revolvers and automatic pistols in the United States. The Colt Co., which is the largest, has devoted 99 per cent of its product to the service of the Nation since the opening of the war, and will continue to so devote an even greater proportion as long as the war

continues. It has postponed, and will continue to postpone, deliveries on commercial orders. Of the small product delivered on commercial orders, 90 per cent has been sold to municipalities and for the protection of essential plants. The same is true of Smith & Wesson and of the Savage Arms Co. Hence, the proposed measure will net no substantial revenue during the war.

THE TAX AS NOW FRAMED PENALIZES THE MANUFACTURERS OF REVOLVERS IN PROPORTION TO THEIR PAST PATRIOTISM.

The Colt Co. now has commercial orders aggregating \$628,991.81 awaiting delivery after the termination of the war. These orders were accepted at flat rates. Hence, as to these orders, the tax can not be transferred to the purchasers. These orders, of which over 85 per cent were accepted prior to the declaration of a state of war, have not been filled because of the outbreak of war the Colt Co., from patriotic motives and at financial loss, immediately devoted its entire plant to the production of arms for the United States and its allies to the exclusion of its commercial business. Because of this patriotic action the Colt Co. will become liable to a special tax of \$157,247.95 on these postponed orders if the bill is passed as now framed. The same situation exists in the case of the other manufacturers.

THE EFFECT OF THE PROPOSED TAX WILL BE TO DISCOURAGE THE MANUFACTURE OF SMALL ARMS IN THE UNITED STATES, AND TO SERIOUSLY IMPAIR THE POWER OF DOMESTIC MANUFACTURERS TO COMPETE FOR FOREIGN MARKETS.

A very material reduction in the sale of revolvers and pistols was the expressed desire of the author of the bill originally proposing this discriminatory tax. (See hearings before the Committee on Ways and Means, House of Representatives, on the proposed revenue act of 1918, Pt. II, p. 1187.) The proposed tax of 25 per cent will increase the retail price materially in excess of that amount because of the increased capital required by the manufacturer, jobber, and retailer, and the interest thereon. All the world, including Germany, will be equipped to manufacture firearms at the close of the war. Hence, imposition of a very heavy, if not prohibitory, tax on revolvers and automatic pistols manufactured in the United States (not for the purpose of raising revenue but to curtail domestic sales) inevitably will result in the substitution of foreign makes in all foreign markets. With domestic sales largely curtailed, and foreign sales virtually eliminated, it is obvious that the manufacture of revolvers and automatic pistols in the United States will practically cease.

THE RESULT WILL BE TO PUT THE UNITED STATES AT A GREAT DISADVANTAGE IN EVENT OF ANOTHER WAR.

The present war is being fought on French soil because Germany was prepared while France and England were not. The great works at Essen had plants, machinery, equipment, carefully trained organizations, and experienced operatives all ready for the immediate production of arms and ammunition in large quantities as soon as war started, largely because the German Government had encouraged the Krupps to build up a great commercial business in guns and munitions in all parts of the world. In France and England (as in the United States) it was necessary to build factories, create machinery, form new factory and arsenal organizations, and train expert ballistic engineers and mechanics before large quantity production could commence. As a result the early armies of Belgium, France, and England were sacrificed—well-nigh totally—and the cause of freedom nearly lost, because Germany had encouraged the commercial manufacture of arms while other nations had not.

Because of the inadequacy of existing plants to supply the American Army with necessary revolvers and automatic pistols, the Government has been endeavoring to create new additional plants for their manufacture; but although we have now been at war 17 months no such plant has been able, as yet, to manufacture a single revolver or pistol. Where would the American Army have received its present supply of revolvers and automatic pistols if all manufacturers of these goods in the United States had been legislated out of existence, as suggested by the author of this provision?

We all sincerely hope that this will be the last war. History warns us, however, not to be too sanguine. Germany is not the only nation which has sought to conquer the world. Clearly it is the part of wisdom to be prepared

against another possible aggression by a mighty robber nation. Reasonable preparedness demands the provision of adequate factory equipment and trained organizations for the immediate production of arms in large quantities. Such equipment and organizations can be maintained only by encouraging the manufacture of such arms during times of peace.

The policy of discouraging the manufacture of side arms, if enacted into law in time of war, can not be altered readily in time of peace. We submit, therefore, that the policy of discouraging the manufacture of side arms by extreme, if not prohibitory, taxation (embodied for the first time in the history of our national legislation in this war revenue bill) is a policy most detrimental to the national interests.

THE TAX IS UNNECESSARY AND UNDESIRABLE AS A POLICE MEASURE.

If it is desired to limit the sale of firearms in certain sections of the country, the proper method for accomplishing that purpose would be by State legislation. The constant carrying of concealed weapons is undesirable, and is limited in most, if not all, civilized countries; but the purchase and possession of revolvers by respectable citizens is desirable and rarely limited in any nation. It affords the best possible protection to the home against night marauders. It trains the citizenry in the accurate and effective use of arms against times of national emergency.

New York State enacted the Sullivan law to discourage such purchases. The result was an increase of 22½ per cent in murders in Manhattan the first year; an increase of 40 per cent in rates on burglary insurance; an open letter from 14 presidents of burglary insurance companies urging its prompt repeal; and a vigorous protest from at least one member of the judiciary. See hearings before the Committee on Ways and Means, House of Representatives, Part II, pages 1190-1194.

We submit that the policy of this discriminatory tax is undesirable, therefore, because it means a perpetuation and extension of the expensive blunder of national unpreparedness; because it will result in centralizing the manufacture of side arms in foreign countries—possibly in Germany; because it will result in penalizing manufacturers in proportion to their patriotic effort in the present war; and because it will increase, rather than decrease, domestic crime. The tax is not designed to, and will not, produce any appreciable revenue during the war.

We submit that the proposed Federal war revenue measures should be so altered as to eliminate this discriminatory and undesirable tax.

Smith & Wesson, of Springfield, Mass.; Savage Arms Co., of Utica, N. Y.; Harrington & Richardson Arms Co., of Worcester, Mass.; and Iver Johnson Arms & Cycle Works, of Fitchburg, Mass., the only other substantial manufacturers of side arms in the United States, authorize us to state that they indorse and join in this protest.

COLT'S PATENT FIREARMS MANUFACTURING CO.
By WM. C. SKINNER, *President*.

The CHAIRMAN. Is Mr. McIntosh in the room?

Mr. MCINTOSH. Yes, sir. Mr. Hedges and I are on the same subject, and by arrangement he precedes me, if that is agreeable to the committee. His name is down, I think, as Mr. Dunham, but it is Mr. Hedges.

The CHAIRMAN. You can proceed, Mr. Hedges.

STATEMENT OF MR. JOB E. HEDGES, REPRESENTING THE ASSOCIATION OF LIFE INSURANCE PRESIDENTS.

Mr. HEDGES. Mr. Dunham obtained this appointment, Mr. Chairman. I represent the Association of Life Insurance Presidents.

The CHAIRMAN. If Mr. McIntosh desires to be heard, you had better divide the time between you.

Mr. MCINTOSH. We do not discuss the same feature at all, Mr. Chairman. I just discuss three or four points apropos of some amendments.

The CHAIRMAN. How much time do you desire, Mr. Hedges?

Mr. HEDGES. I will be much more modest than any one you have heard to-day.

The CHAIRMAN. We have heard some pretty long ones and some pretty short ones.

Senator PENROSE. Mr. Hedges is a speaker of national reputation, Mr. Chairman.

Senator THOMAS. I think Mr. Hedges will not impose upon the committee.

Mr. HEDGES. Apropos of what I heard when I was here yesterday before the committee and to-day, I have committed to writing the substance of what I have to say to the committee, which I will ask to have incorporated in the record as if spoken. There are only a dozen pages, and there are just one or two points I want to emphasize orally, and if you people will just take it for granted that the character of our Association of Life Insurance Presidents is as good as other people say theirs is, and we all want to win the war equally, and that we can not understand the structure of this bill, we will save time. [Laughter.] If you will give me credit for that good character before you start, we will save time.

The first thing which I have to suggest is the modification of one or two sections of the bill.

The substitution of the new individual and corporate income taxes for like taxes imposed by the acts of 1916 and 1917 should be stated explicitly. That is this bill, as I understand it, seeks first to raise by means of income taxes or other special taxes the additional revenue required by the exigencies of war; and, second, to consolidate and codify into a single act all of the existing income taxes and other special taxes which are applicable to the tax-paying public.

Regarding all the amendments that have been made or that have been sought to be made on each section, except the two sections with reference to insurance, they have all started with the words "in lieu of." It may have been overlooked in reference to these insurance matters, and possibly was, and therefore I have suggested, in regard to sections 210 and 230, that there just be added, for the sake of symmetry of construction, the words "in lieu of," so that there may be no doubt by way of later argumentative discussion whether this was supplementary or added to or subtracted from. This is simply to put it on an equal basis as a matter of physical construction.

As to the other thought, I wish to emphasize to the committee the proposition in the bill that the income-tax rate should be modified or eliminated. I am going to digress and do what is otherwise an unintelligent thing to do, and read from a manuscript in order to be exact. That has already been touched upon in a general way by some of the other gentlemen here, the proposition now being, in a word, while all corporations are sought to be characterized in the single phrase "as such," it is impossible in fact to characterize them accordingly, and logically so in the case of insurance companies, for this reason: The tax being raised to 18 per cent, the committee of the House sought to reduce to 12 per cent the rate of tax in those instances where a surplus was paid out for obligations, or by a declaration of dividends.

The former method is not open to these insurance companies at all. They do not carry a bonded indebtedness, and therefore they have no means of taking advantage of that particular thing.

On the question upon the matter of the paying of dividends, as you all know, and as has been argued here to-day, an insurance dividend is different from any other dividend.

The Government makes announcement to the insurance companies that in order to make the process easier and to get the advantage of that 6 per cent differential, this money that is a part of surplus funds will be disbursed so that a credit of 6 per cent can be gained, provided that money is taken away from the individual recipient where the process is less painful and applied to surtaxes. That might be possible providing the theory and practice of life insurance as such were abandoned. As we all know, this question of a reserve is the exact thing which makes a policy solvent, if nothing else happens. I can see, from my own standpoint, whether it is logical economically or not, that to the man who pays that premium which gives life and validity to the perpetuity of that policy, as a mental operation he is entitled to know mentally, as well as to have it served to him administratively, that his policy is good. That adds to the economic, potential forces of the United States without question. Therefore, to enable those people to avoid the penalty of a 6 per cent differential against them, they would have only one of the two recourses which are open to other people, namely, the dispersion of that surplus which is an added security to cover a war such as we are now in. An added security above the original conception.

All the States recognize, as a matter of fact, the existence of a surplus above a reserve as desirable, and some of them by statute—some six or seven, and particularly New York—recognize it and say it should not go above something. Up to something it is all right. Above that it would be perhaps extravagant. Therefore this differential, so far as life insurance companies go, distorts the original conception that governs toward this particular line of activity, because there is a difference when a man parts with his money for merchandise, and when he purchases a credit or debit obligation running from another person to him, which will continue provided he does something. He is more apt to do that something which keeps this contract alive when he is assured in his mind that that will be continued by this direction.

The Government has gone into the insurance business, which is all right. Most of these policies that are now in existence were written before this war started. Those that were written subsequent to the declaration of war have provisions in them which are protective. There are certain general features, but when you come to analyze the physical workings of a business the difficulty of characterizing a number of corporations under a single phrase is almost beyond conception.

After we had had in New York our original insurance investigation, which revived many of the standards both as to security and administration, the report of the committee, which furnished the groundwork of most of the insurance legislation of many of the States, contained this language at page 320 [reading]:

However, as the precise results of the continuance in business can not be predicted and as investments may fall as well as raise in value it is important that the company should be provided with a contingent fund for the security of its policyholders and should be permitted to accumulate such a fund out of its surplus.

In each one of these original jurisdictions, of all the businesses they have regulated there is none regulated more potently and exactly than this, not excepting banking. Now, it is in the statutes, as we all know, that savings banks and fraternal organizations are not taxed, and there is no question about it.

Senator THOMAS. Right there, what legal reason can we assign, Mr. Hedges, for the exemption of these fraternal societies that does not apply to strictly mutual life insurance companies? I am unable to see any.

Mr. HEDGES. If the record could say that the witness stood mute, you would get me in less trouble.

Senator THOMAS. Well, I think I know what the answer would be as to the real reason, because I have expressed myself.

Mr. HEDGES. I do not raise an argument for myself, but it is something worth sentimentally taking into consideration when, by virtue of conditions which these life companies can not obviate by virtue of the limitation, they can not take advantage of that.

If anyone should inquire of me if I have to suggest any amendment, I have one, and it coincides with the gentleman referred to here several times—the Secretary of the Treasury—and I suggest that it comes very aptly in connection with the purchase of these bonds that are coming out.

Let them get credit for those. In order to free the bill from this objection which I have spoken of in a general way, you can incorporate in this section, paragraph A of section 230, after the word "year" in line 3, on page 32 of the bill, the words "the amount invested in obligations of the United States issued after September 1, 1918."

You see, if there were a transaction which was entirely concluded by the payment of a sum of money and the transfer of a bit of merchandise, and if the surplus of these insurance companies and the surplus of a corporation in ordinary merchandising business bears the same relationship to the continuity of the business in each case, it would be useless for me to be here.

Mr. McIntosh will address the committee on the subject of deferred dividends, which is entirely different from what I have been discussing.

There is a new proposition in this present bill which possibly, as a matter of cold-blooded logic, may be none of the business of these insurance companies. It is a policy of the Government that follows the payment of a death claim, and yet it is within the penumbra of insurance business. That has been brought about, as Mr. Kitchin says in his report, by the fact that many letters sent the Treasury Department tend to show that agents have asked for the investment in insurance policies for the purpose of removing money to a point where it could be taxed by the Government; in other words, of a payment of a large level premium for a large amount of insurance.

That goes, generically, if the committee will bear with me for just a moment, to this proposition: Is it or is it not a good proposition that insurance, as such, may be used for the protection of an estate and the yielding at once, without sacrifice, of securities in the collection of taxes, whether they are Federal, State, or local? Is it not desirable to provoke the people as a part of their insurance invest-

ment, adding to what they would ordinarily take in a life policy from everyday experience, to take some more so that sometimes when that instant comes that the estate is to be liquidated the beneficiary or the executor charged with the trust responsibility shall have funds without throwing on the market securities or selling real estate referred to by Mr. Kitchin himself in this printed syllabus?

In working that out the House committee has made an exemption of \$40,000 totaled as against any one man who has insured his own life in favor of individual beneficiaries. I have not been long enough in the atmosphere of the companies to know, but my guess would be that the average every day, rough and tumble policy was a small policy—

Senator JONES. Is that any different from many other things that might be considered laudable? Suppose a man is getting along in life and does not own a home, and he wanted to leave his wife a home. Would you say that money invested in a home for the wife, income invested in a home for the wife, should not be taxed?

Mr. HEDGES. Should I say that money left to protect her should not be taxed?

Senator JONES. No; to buy a home. He has not a home, and a man ought to leave his wife a home. He takes his income and buys a home for his wife. Is not that a very laudable thing to do? Would it not be just as equitable to exempt that income from taxation as it would be in the case where a man buys a life insurance policy?

Mr. HEDGES. The analogy is apparent; but this is the thought I want to leave: Do I understand you to mean, Senator, that if a man leaves his money for that purpose, or makes provision before he dies—

Senator JONES. Makes provision before he dies.

Mr. HEDGES. Yes; entirely desirable.

If the Government feels, through its committee of the House, or later through this committee, that there has been a condition which could be reached by Government money invested in life insurance which has diverted an income in some way from the Government—I just make this suggestion. There might be a difference of opinion about it, but I hardly think so; that is, to switch the exemption from the proposition of \$40,000 to the amount that may have been invested in an insurance risk; in other words, to the extent of the excess, referring back to that section, of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life, "over such sum as may be necessary to defray the estate tax imposed by this title and any State transfer or inheritance taxes which may be imposed upon the decedent's estate, and to the extent of the excess over \$40,000 of the amount of premiums paid by the decedent for insurance taken out upon his own life subsequent to January 1, 1917, in favor of all other beneficiaries."

In other words, the Government either wants to punish an agent, disturb and stop a practice which it thinks wrong, or has not any definite plan—

Senator SMOOT. The latter is the case in the bill as it is constructed now.

Mr. HEDGES. I suggest that. I do not know that it is within my purview even to suggest it.

Senator SMOOT. The suggestion is all right, but I could not quite follow it. I would like to have you state it again. I can read it after it is in the record, however.

Mr. HEDGES. What I have done here, so as not to take undue time and make a long brief for everyone to read, has been to take some 13 or 14 pages, and I have taken on each page a letter reference to a letter amendment and line, and at the back of it I have put on a separate page the entire section as it would be when amended.

Senator SMOOT. That will be sufficient. I do not want to discuss it. I tried to follow your statement, and I could not quite do so.

Mr. HEDGES. So far as those three propositions are concerned, everything is in there, unless some one on the committee should want some information regarding a specific feature of it.

Senator THOMAS. Mr. Hedges, is not every tax levied upon a strictly mutual life insurance concern a tax upon the beneficiaries, and to that extent an increase in the cost of insurance?

Mr. HEDGES. Exactly.

Have you absolved me, Mr. Chairman, for taking time unduly?

The CHAIRMAN. You talk so interestingly—

Mr. HEDGES. I would like to get a clean bill of health before I leave, because you looked yesterday, once or twice, as if you did not have confidence in the ability of the speaker to conserve time.

The CHAIRMAN. You have the ability of presenting a matter very forcefully.

Mr. HEDGES. Thank you very much, sir.

(A statement was submitted by Mr. Hedges and is here printed in full, as follows:)

AMENDMENTS OFFERED BY ASSOCIATION OF LIFE INSURANCE PRESIDENTS.

LIFE INSURANCE COMPANIES DO NOT SEEK EXEMPTION FROM ANY TAX IMPOSED UPON THEM BY THE BILL.

The income tax and excess-profits and war-profits taxes imposed by the bill are expressly made applicable to insurance companies to the extent that such companies have taxable income or realize excess profits or war profits. In this respect life insurance companies are on precisely the same footing with every corporation. The special tax on new business which was a feature of the act of 1917 is also continued in force by this bill. The companies, however, expect cheerfully to make such contributions to the needs of Government as the Congress may, in its wisdom, prescribe. Our intention, therefore, is to limit this discussion of the bill to constructive criticisms of certain provisions—chiefly of general application—which appear to merit special attention.

It is understood that the Congress intends to impose the necessary taxation in accordance with principles of justice and fairness and sound public policy, and that this committee is here to receive the views of taxpayers as to the operation and effect of such of the provisions of the bill as may be deemed to be in any respect unequal, unfair, or impolitic, for the purpose of its information and with a view to the possible amendment of the bill.

Life insurance corporations are, intrinsically, merely cooperative agencies for the accumulation by their policyholders or members of funds for the mutual payment of specific benefits in event of death or other specified contingencies. With the exception of the guaranty fund or capital stock contributed by the stockholders of companies organized upon the capital-stock plan, or by the guarantors in the case of certain mutuals, all of the funds of a life insurance corporation are contributed by its policyholders. Life insurance itself is a facility afforded the living to provide, after their decease, for their dependents. It involves a pecuniary sacrifice by the person insured, which has been aptly described as a self-imposed tax and indirectly inures to the benefit of the State.

In innumerable cases life insurance is all that stands between a beneficiary and absolute destitution. Without it the dependents of the average citizen would become, for a time at least, either objects of private charity or charges upon the public. The importance of life insurance has recently received at the hands of this very Congress the most effective official indorsement possible through the amendment to the war-risk insurance act, which authorizes the issuance by the Treasury Department of policies of life insurance to the soldiers and sailors engaged in the present war.

That life insurance should not, on principle—by reason of its quasi public and beneficent character—be taxed it seems unnecessary to argue. This very bill recognizes the impolicy of taxing kindred institutions, to wit: Savings banks and fraternal and assessment-associations, as well as various other cooperative agencies for mutual benefit, which are expressly exempt from taxation thereunder. We do not, however, advert to this fact for the purpose of asking that taxes like those borne by the life insurance companies be imposed upon these institutions. Believing that all similar disinterested agencies for the common good should be exempt, we are content that they should be exempt. Moreover, realizing the need of the Government for revenue in the present emergency, we are not asking to be relieved at this time from either the general taxes or from the special tax on life insurance which are imposed by the bill. Our purpose is simply to ask that the bill be so amended in certain particulars as to supply obvious omissions in the present draft or to bring it into accord with principles of sound public policy, which, incidentally, in one instance only, will also involve the abatement of an unintentional discrimination against life insurance.

THE SUBSTITUTION OF THE NEW INDIVIDUAL AND CORPORATE INCOME TAXES FOR LIKE TAXES IMPOSED BY THE ACTS OF 1916 AND 1917 SHOULD BE STATED EXPLICITLY.

It has been generally understood that the purpose of the bill was twofold: First. To raise, by means of income taxes or other special taxes, the additional revenue required by the exigencies of the war. Second. To consolidate and codify into a single act all of the existing income taxes and other special taxes which are applicable to the taxpaying public.

This second purpose was well calculated to afford the taxpayers relief from the labor and confusion which is necessarily involved in following the intricacies of previous acts and more recent supplements in order to determine the nature and amounts of the various taxes applicable to themselves. It should be noted, however, that neither the revenue act of 1916 nor that of 1917 has been explicitly repealed.

The method employed in the bill to relieve the taxpayers subjected to the various special taxes included in the bill from like taxes imposed in the earlier acts has been to include in the clause which imposes such taxes a provision to the effect that the tax thereby imposed shall be in lieu of the corresponding tax imposed by the earlier acts. For example, with respect to the war-profits and excess-profits taxes it is provided by section 301 of the bill that the tax imposed thereby shall be "in lieu of the tax imposed by Title II of the revenue act of 1917." Similarly by section 401 it is provided that the estate tax thereby imposed shall be "in lieu of the tax imposed by Title II of the revenue act of 1916 and Title IX of the revenue act of 1917"; and by sections 500 and 503 it is provided that the special taxes on transportation and other facilities and on insurance imposed thereby shall be in lieu of the taxes imposed by the corresponding sections of the revenue act of 1917. This method seems to have been consistently pursued by the draftsmen of the bill with respect to all of the existing taxes, which it is proposed either to continue or increase by the bill, except only in the case of the corporation income tax and the normal income tax applicable to individuals; and with respect to the normal tax on individuals the committee report which accompanied the bill explicitly states that:

"In lieu of the rates now in effect the proposed bill [sec. 210] levies upon citizens and residents of the United States a normal tax of 12 per cent upon the amount of the net income * * *."

It is, therefore, clear that the failure of the bill to include provisions to the effect that the normal income tax and surtaxes imposed upon individuals and the corporation income tax are in lieu of the like taxes imposed by the former acts was due to oversight. We think, however, that in order to avoid any misapprehension as to the intent in this matter it should be expressed in ex-

pllicit terms in the appropriate sections of the bill in the same manner as it has already been done in the case of the other taxes. For the convenience of the committee we offer the following specific amendments:

To section 210: After the word "That" in line 13 on page 5 of the bill insert: "In lieu of the taxes imposed by section 1 of the revenue act of 1916 and section 1 of the revenue act of 1917, but in addition to all other taxes imposed by this act."

To section 230: After the word "That," in line 17 on page 31 of the bill, insert: "In lieu of the taxes imposed by section 10 of the revenue act of 1916 and section 4 of the revenue act of 1917, but in addition to all other taxes imposed by this act."

THE DIFFERENTIAL FEATURE OF THE CORPORATION INCOME-TAX RATE SHOULD BE MODIFIED OR ELIMINATED.

The subject of the differential income-tax rate which is made applicable to corporations under section 230 has already been discussed before this committee by representatives of various mercantile and manufacturing corporations. We therefore assume that the committee has been sufficiently acquainted with the general nature of the objections to which this principle is open upon economic as well as practical grounds. Our endeavor will be to show the committee the un wisdom of applying the differential rate to insurance companies, by reason of the peculiar nature of the insurance business.

Although the first clause of this section establishes 18 per cent as the normal rate of tax upon the net income of corporations, this clause is immediately followed by the proviso—

"That the rate shall be 12 per cent upon so much of this amount as does not exceed the sum of (1) the amount of dividends paid during the taxable year, plus (2) the amount paid during the taxable year out of earnings or profits in discharge of bonds and other interest-bearing obligations outstanding prior to the beginning of the taxable year."

The effect of this proviso may readily be anticipated. It will be to establish as the rate of income tax on corporations, as matter of practical fact, a rate of 12 per cent instead of 18, through the process of placing a premium upon the immediate distribution of corporation income. The draftsmen of the bill not only realized but intended this. Chairman Kitchin states in his report:

"The committee believes that the reduction of the rate to 12 per cent on an amount equal to the amount of dividends paid will have a wholesome effect in many cases in stimulating the payment of dividends, which will be subject to surtax in the hands of the stockholders." (P. 12.)

There are two objections to this differential rate from the point of view of insurance. The first objection is founded upon the principle that equality is equity. Insurance companies have no bonded or interest-bearing indebtedness, and mutual insurance companies have no capital stock and, consequently, pay no dividends, as defined in the bill. A discrimination, therefore, results as against insurance corporations in the practical rate of tax applicable to them, as contrasted with the rate which will be paid by other corporations under this provision.

The second objection, from the point of view of insurance, is that it is peculiarly against public policy to encourage, or, as does this provision, practically compel the dissipation by insurance companies of the entire amount of each year's surplus, a substantial portion of which, it is recognized by the State laws governing insurance and by the rulings of supervising insurance officials of the various States, should be added to the working capital of the companies for the further guaranty and protection of their policy contracts.

It should be borne in mind by the committee that the relation of the public to insurance companies differs from their relation to ordinary business concerns in this fundamental respect: An insurance company has no commodity to sell and deliver upon payment of the purchase price. On the contrary, in consideration of a substantial cash payment made to it in advance an insurance company merely binds itself to make some stipulated payment at some future time in event of some stipulated contingency. In other words, while the transaction is practically completed when an individual pays over to an ordinary corporation the purchase price of a commodity sold or service rendered, in the case of an insurance company, so far as the individual is concerned, the practical relation of creditor has been established as between himself and the corporation, which imparts to him a vital interest in the financial stability of the corporation. For this reason, as in the case of banks of deposit, we think it is clear

that insurance companies should be encouraged, rather than discouraged, from setting aside such proportion of their gains from each year's operation as the management of each individual corporation may deem proper.

While the legal reserves of life insurance companies are mathematically sufficient to insure the performance of all obligations assumed under ordinary circumstances, the possibility of unusual contingencies, however remote that may be, must be reckoned with. Upon this point the Armstrong committee of the New York Legislature, which made a very thorough study of the subject of life insurance in 1905, said, at page 320 of its report:

"However, as the precise results of the continuance in business can not be predicted, and as investments may fall as well as rise in value, it is important that the company should be provided with a contingent fund for the security of its policyholders and should be permitted to accumulate such a fund out of its surplus."

One of these contingencies which the company managers have always had in mind is the possible decrease in the value of securities in which the legal reserves are invested. Another is the occurrence of excessive death losses through epidemic or war, which might disturb the calculations upon which the premiums charged for the insurance afforded were based. Both of these contingencies immediately confront the companies to-day. But for their surpluses, against the accumulation of which this differential rate is, we think, unwittingly directed, some of them might not survive the period of this war without serious impairment and corresponding loss and distress to their policyholders.

It is, therefore, clear that amendment of this section, at least to the extent of obviating this result, is necessary. The amendment which we suggest would be to include in the aggregate of income subject to the 12 per cent tax so much thereof as might be invested in Federal Government bonds. In order to free the differential rate from the objections noted, we would suggest the incorporation of the following:

In paragraph (a) of section 230, after the word "year," in line 3, on page 32 of the bill, insert: "plus (3) the amount invested in obligations of the United States issued after September 1, 1918."

THE PROCEEDS OF LIFE INSURANCE SHOULD NOT BE REDUCED BY THE ESTATE TAX.

The average individual seeks insurance for one or both of two reasonable and commendable purposes: First. To make specific and certain provision for dependents. Second. To provide a fund which will defray the expenses of the administration of his estate. These purposes, we believe the committee will agree, should be encouraged by the Government.

With the increase in the need of governments for revenue, taxes on decedents' estates have become exceedingly onerous. States vie with the Federal Government in the imposition of this burden and the taxes are becoming increasingly heavier. The Federal estate and the State transfer or inheritance taxes have thus come to be by far the largest items involved in the expense of administering even modest estates; and these taxes must be paid in cash. It will, moreover, doubtless be conceded, that under ordinary circumstances the most unfavorable occasion for the conversion of an estate, or any considerable proportion thereof, into cash is that following the death of its owner and responsible manager. If not a practical impossibility, it would certainly be a serious economic and pecuniary loss for any man to be compelled at all times to retain on hand a fund sufficient for the payment of the inheritance taxes upon his estate. The story of the master's rebuke to the slothful servant who kept his talent unemployed illustrates the principle involved. On the other hand, the immediate realization of cash from unliquid investments, except at an improvident sacrifice, would be impossible. The process in many instances would take years if serious loss were to be avoided. The House committee says at page 23 of its report:

"In the case of those estates where the holdings of the decedent are largely in lands and other property for which there is no ready market it has been found in practice that a forced collection of the tax results in enormous sacrifice to the beneficiaries."

The situation has a public aspect as well. Necessity for the prompt administration of considerable estates will seriously depress the values of the securities and other property which the process throws upon the market for immediate liquidation.

The only practical way in which a fund can be provided for the payment of those taxes without economic loss to the State as well as pecuniary loss to the

individual is through the medium of life insurance. By this means the necessary money can be rendered available without the disturbance of business, without hardship to individuals, and without delay to the Government; and the resort to insurance for this purpose should, we submit, be encouraged rather than discouraged by the exemption of the proceeds of such insurance from the estate tax. The necessity of providing by insurance for a heavy tax upon the proceeds of the policy itself, in addition to the tax on the estate, is confusing. It appears like piling Pelion on Ossa to the bewildered taxpayers and the cost becomes prohibitive.

The other purpose for which life insurance is ordinarily procured, namely, for the protection of dependents, should also be encouraged. Instead of offering encouragement the bill extends the application of the estate tax to the proceeds of life insurance in excess of \$40,000 payable to individual beneficiaries. The committee's report (at p. 22) indicates that this provision was inserted in the belief that men of wealth were converting their estates into life insurance for the purpose of their transmission free from the tax. If such be the fact, we agree that an adequate check to the process should be established. Such remedy, however, should be directed solely at the evil sought to be cured.

The danger of injustice inherent in a provision which would tax the proceeds of life insurance to individual beneficiaries under the estate tax was recognized by the House committee. The exemption of \$40,000 in insurance benefits, which was intended to obviate this danger, would not in many instances be sufficient.

Having in mind the purpose of the framers, to prevent the conversion of assets which would otherwise be subject to the estate tax into nontaxable life insurance, it would seem that the proper remedy is to tax, not the insurance which results therefrom, but the assets so diverted. In other words, the taxation of the premiums paid by a decedent in excess of such amount, either annual or aggregate, as the committee may deem reasonable, for insurance payable to individual beneficiaries, would seem to be the proper remedy.

In view of the foregoing considerations we therefore propose the following amendments:

To paragraph (f) of section 402 of the bill: After the word "extent," in line 14, at page 71 of the bill, insert "of the excess." After the word "life," in line 16, at page 71 of the bill, insert "over such sum as may be necessary to defray the estate tax imposed by this title and any State transfer or inheritance taxes which may be imposed upon the decedent's estate."

In line 17, at page 71 of the bill, strike out the words "receivable by all other beneficiaries," and insert in lieu thereof "of premiums paid by the decedent for."

In line 18, at page 71 of the bill, strike out the words "under policies."

After the word "out," in line 18, at page 71 of the bill, strike out "by the decedent"

After the word "life," in line 18, at page 71 of the bill, insert "subsequent to January 1, 1917, in favor of all other beneficiaries."

The several amendments herein above suggested are appended hereto in form showing graphically all proposed changes; matter omitted inclosed in brackets and new matter underlined.

PROPOSED AMENDMENTS.

[Explanation: Matter underlined is new; matter in brackets is language of bill omitted.]

PROPOSED AMENDMENT TO SECTION 210 OF PENDING REVENUE BILL (H. R. 12863) RELATIVE TO THE NORMAL INCOME TAX ON INDIVIDUALS.

SEC. 210. That in lieu of the taxes imposed by section 1 of the revenue act of nineteen hundred and sixteen and section 1 of the revenue act of nineteen hundred and seventeen, but in addition to all other taxes imposed by this act, there shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax, as follows:

PROPOSED AMENDMENT TO SECTION 230 OF PENDING REVENUE BILL (H. R. 12863) RELATIVE TO NORMAL INCOME TAX ON CORPORATIONS.

SEC. 230. That in lieu of the taxes imposed by section 10 of the revenue act of nineteen hundred and sixteen and section 4 of the revenue act of nineteen hundred and seventeen, but in addition to all other taxes imposed by this

act there shall be levied, collected, and paid for each taxable year upon the net income of every corporation a tax as follows:

PROPOSED AMENDMENT TO SECTION 230 (A) OF PENDING REVENUE BILL (H. R. 12863)
RELATIVE TO THE INCOME TAX ON CORPORATIONS.

(a) In the case of a domestic corporation 18 per centum of the amount of the net income in excess of credits provided in section 236: *Provided*, That the rate shall be 12 per centum upon so much of this amount as does not exceed the sum of (1) the amount of dividends paid during the taxable year plus (2) the amount paid during the taxable year out of earnings or profits in discharge of bonds and other interest-bearing obligations outstanding prior to the beginning of the taxable year [:], *plus* (3) *the amount invested in obligations of the United States issued after September first, nineteen hundred and eighteen:*

PROPOSED AMENDMENT OF SECTION 402 (F) OF PENDING REVENUE BILL (H. R. 12863)
RELATIVE TO THE ESTATE TAX.

(f) To the extent of the *excess* of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life [:] *over such sum as may be necessary to defray the estate tax imposed by this title and any State transfer or inheritance taxes which may be imposed upon the decedent's estate;* and to the extent of the excess over \$40,000 of the amount [receivable by all other beneficiaries as] *of premiums paid by the decedent for insurance [under policies] taken out [by the decedent] upon his own life subsequent to January 1, 1917, in favor of all other beneficiaries."*

Respectfully submitted.

ASSOCIATION OF LIFE INSURANCE PRESIDENTS,
JOB E. HEDGES, FREDERIC G. DUNHAM, *Of counsel.*

NEW YORK CITY, September 12, 1918.

The CHAIRMAN. We will now hear from Mr. James H. McIntosh.

STATEMENT OF MR. JAMES H. McINTOSH, GENERAL COUNSEL,
NEW YORK LIFE INSURANCE CO.

Mr. McINTOSH. Gentlemen, Mr. Hedges has left it for me to present to the committee a suggestion by amendment to the bill in which he and all other insurance companies interested in the subject concur in suggesting the amendment. The amendment is this, that they ask to have stricken out, on page 35 of the bill, the paragraph commencing at line 11 and terminating at line 16, the paragraph which commences:

"In the case of life insurance companies there shall not be included in gross income such portions," etc.

They ask to have that paragraph stricken out.

On page 39, in line 15, we ask to have stricken out the words "other than dividends," so that the clause will read, when the amendment suggested is made, the clause relating to deductions: "and (b) the sums paid within the taxable year on policy and annuity contracts."

When that amendment is made the law will clearly show that insurance companies are to do what they all hitherto have done in making their returns under the law ever since, in 1913, the paragraph contained on page 35, which I have asked to have stricken out, was first inserted in the income-tax bill.

The reason why we wish this amendment made is, first, that it will qualify the law, and second, that it will avoid a discrimination between corporations of the same kind and class based upon the forms of contracts they make, if the construction of the paragraph

on page 35 which the revenue department has put upon it is sustained by the courts.

Read the first paragraph that we ask to have stricken out and see what it means. It means nothing at all if you construe it literally, because no insurance company ever paid back in any year any part of a premium which they received in that year, and that is the literal reading of the paragraph.

So that if you construe it literally, it means absolutely nothing. When it was put in the bill in 1913 we were called upon to construe it, and we did so in the light of the situation that obtained at the time that amendment was put in the law of 1909, and in the light of what had transpired between 1909 and 1913 with respect to the subject we thought was intended to be treated in that paragraph. The law of 1909 had in it the paragraph contained on page 39, out of which I ask to have the words "other than dividends" stricken.

One of the important insurance companies in making its return to the Government did not deduct the dividends as a deduction, but they did not include as income any part of the dividends paid by them which were used in the abatement of premiums, because they claimed that to that extent those dividends were not income received by the company. The Treasury Department reviewed their tax returns and said they were wrong in not reporting those dividends as income assessed and taxed accordingly, which they paid under protest and sued to recover it back. That suit was determined in the Federal court in New Jersey in 1912—

Senator THOMAS. How was it determined?

Mr. McINTOSH. Judge Ross, of that court, held that the dividends were not income received by the company, but were merely overpayments of premium made by the policyholder, which the company was to account to him for, and constituted a return to the policyholder of his own money after the company, at the end of the year, had taken an account of its business and found out how much he had overpaid them.

Judge Ross's opinion in that case gives a very lucid and illuminating exposition of the true theory of life insurance.

Senator DILLINGHAM. Where can that be found?

Mr. McINTOSH. That is in 198 Federal Reporter at page 199.

Senator THOMAS. What is the title of the case?

Mr. McINTOSH. Mutual Life against Herold, 198 Federal, 199.

The Federal Government took that case to the court of appeals, and it was decided in January, 1913. The court of appeals sustained the ruling of the lower court and adopted the opinion of Justice Ross as the opinion of the court of appeals, except that they qualified it in some respects on features which Judge Ross had discussed, but which were not really in issue in the case. But in a short opinion rendered by the court of appeals in affirming the decision of the lower court the court said in almost these words—I regret that I do not have the volume here to read it to you so as to give it to you precisely. I tried to get it here, but I was told I could not get it nearer than the Capitol—

These dividends paid annually are overpayments of the policyholder and are not income at all.

On the faith of that decision and on the faith of what the committee, in reporting the act of 1913, said about this paragraph when

they inserted the paragraph in the 1913 act, we understand that by this amendment of 1913 the Congress intended that life insurance companies doing business on the mutual plan should not include dividends as income, and have acted on that construction of the law from that day to this, and that construction of the law has been sustained in a case directly involving it, decided by the United States district court at Philadelphia, entitled *Penn Mutual Life Insurance Co. v. Lederer*, reported in Two hundred and forty-seventh Federal Reporter at page 559.

Senator THOMAS. Did you present this feature of the bill to the Ways and Means Committee?

Mr. McINTOSH. No, sir; I did not. I spoke about it to one or two members of the committee and got the impression that there would be no question about the amendment being made, and I did not know that it was not made until I saw—

Senator THOMAS. Give me that citation again, please.

Mr. McINTOSH. *Penn Mutual Life Insurance Co. v. Lederer*, Two hundred and forty-seventh Federal Reporter, page 559.

That opinion also is a very illuminating opinion. Under the construction which we have thus put upon the law, the New York Life Insurance Co. has paid the Federal Government very important sums as taxes. Our tax for 1918 on the business of the year ending December 31, 1917, under this law, as construed in the way I stated, was \$409,113.74. But the department, after hesitating for something like four years, in a ruling made on the 27th of March, 1917, does not concur in that construction of the statute. The department says that this clause which we ask to have stricken out authorizes not including in income the annual dividends, but as to deferred dividends it requires those to be included except so much thereof as actually used in the payment of premiums in the year in which the dividend was paid. That is a negligible sum, so small that it is scarcely worth the clerical work required by the companies to ascertain the amount of it. It is 3 or 4 per cent of those dividends.

So that that clause as construed by the department discriminates between companies which have always done an annual dividend business on the one hand and companies that have done a deferred dividend business on the other, by allowing the annual-dividend companies to deduct all of their dividends and the deferred-dividend companies to deduct no part of the deferred dividend except the trifling amount that was used in the dividend year for the liquidation of a premium that year.

See what that means—and this affects, so far as dividend companies are concerned, a large number of companies. On the other hand, it affects companies who have never done anything but an annual dividend business. So far as New York companies are concerned they all have done nothing but an annual-dividend business since January 1, 1907; but before that time practically all New York companies did a deferred-dividend business. But several important and great companies have never done a deferred-dividend business at all, but have always done an annual-dividend business. So that as to those companies their entire dividend fund by the department ruling is not included in income. As to these other companies, only such contracts as they have outstanding for an annual dividend fund get the benefit

of the act, whereas all of their outstanding contracts which are on the deferred-dividend plan are included in income.

I want to show you just how that comes about——

The CHAIRMAN. Mr. McIntosh, I think the committee would be very glad to hear your general proposition, and, if you have authorities, to have you cite them; but, really, we have not the time to have an elaborate speech from you in discussion of these questions. There are other gentlemen here whom we must hear this afternoon, one especially who has got to leave here to-night, and if he can not be heard this afternoon he can not be heard at all.

Mr. McINTOSH. May I have 10 minutes to give these figures?

The CHAIRMAN. Yes.

Mr. McINTOSH. Thank you.

The CHAIRMAN. We are very anxious to give you all the time we possibly can in justice to these other gentlemen who are here and who desire to be heard.

Mr. McINTOSH. I understand perfectly.

I want to show just what the extent of this discrimination is by taking the figures of my own company for this year.

On our construction of the law we have paid tax this year, as I have already said, of four hundred and nine thousand and odd dollars. I have got a photograph of our return here. If we be assessed on the construction of the department, we have to add to that a sum of \$699,966.40.

So that if we were an annual-dividend company to-day, whereas our tax was \$409,000, because part of our business is on the deferred-dividend plan our tax under the department's construction here would be \$1,109,000 for 1918 on the business of 1917. In other words, we are discriminated against as between the New York Life as a mutual company and because it has deferred the dividend policies in a tax for this year of \$700,000.

There is an element of discrimination in this on account of the deferred-dividend fund that is unintentional, but which we do not object to because it is within the purview of the law. That is, that this deferred-dividend fund is in our hands and a part of our income arises from it.

For instance, in 1917, at the beginning of the year, we had a deferred dividend fund of \$87,000,000 that is held for distribution and return to these policyholders. Our interest earning was about 4½ per cent on all our invested funds. The income from that deferred dividend fund was \$3,929,000. On that we paid a tax this year, and make no complaint about it, of \$235,000, which is included in the \$409,000 which we paid.

Now, that is a discrimination which we have to suffer from the construction of the bill——

Senator SMOOT. Ultimately does the man who has paid that deferred dividend fund receive every dollar of it that he has paid in it or is there only a portion of it that goes back?

Mr. McINTOSH. He receives every dollar that he paid in with the accumulations, and these are the accumulations that we paid the tax on. So that a policyholder who pays on a deferred dividend policy is a policyholder in a mutual company, and his overpayments are held, and that is why Congress said whether they shall be paid back, credited, or treated in abatement of premium. We credit it, and

we want not to include it as income, and that is the whole case, and that is why we ask that amendment.

Thank you very much.

(The chairman here submitted a letter on the subject of life insurance, which is printed in full, as follows:)

MASSACHUSETTS MUTUAL LIFE INSURANCE Co.,
Springfield, Mass., September 21, 1918.

Hon. F. M. SIMMONS,
Senate Building, Washington, D. C.

MY DEAR SIR: I am not writing at the instigation of anyone. My motive is to endeavor to correct what I deem an inequality in House bill 12863, which, if not corrected, will affect hundreds of small corporations adversely, and will practically eliminate the sale of corporation life insurance, which has almost reached the point of being an economic necessity as a business steadier, as well as assuring the perpetuation of a corporation.

Should the proceeds arising from a life insurance policy at the death of the insured when said policy is made payable to a corporation be taxable in excess of premiums paid as corporation income, excess profit, or war profit, as the case might or may be?

Can the death of a valuable officer or employee of any corporation, even if his life is insured in favor of said corporation, ever be justly looked upon as an excess profit or war profit?

The proceeds of a policy of life insurance, over and above premiums paid under cases similar to the ones interrogated in the two preceding questions, might justly be determined to be income, but could not justly be treated as an excess profit or a war profit.

It is unfair to any corporation who carried corporation life insurance to leave section 213 to be worded as it is in lines 14, 15, and 16 of Union Calendar 256, H. R. 12863, which lines read as follows:

"The proceeds of life insurance policies paid upon the death of the insured to individual beneficiaries or to the estate of the insured."

This is under the section headed "Gross income defined," and is one of the exemptions made under gross income. And then to turn to "Gross income defined for a corporation," on page 35, section 233, which reads that in the case of a corporation the term "gross income" means the gross income as defined in section 213. The question revolves as to whether a corporation that was a beneficiary under a life insurance policy would be included as an individual beneficiary. By striking out the word "individual" and substituting "any beneficiary" the uncertainty is corrected, and the proceeds of corporation life insurance policies would be specifically exempted from gross income.

I wish you to bear in mind that on page 17 of said bill, "Items not deductible," line 20, and following, reads in this manner:

"Premiums paid on any life insurance policy covering the life of any officer or employee or of any person financially interested in any trade or business carried on by the taxpayer when the taxpayer or anyone financially interested in such trade or business is a beneficiary under said policy."

The result of this wording is that a corporation could not charge a corporation life insurance premium to expense.

If the death occurs of an officer or valuable employee of a corporation carrying corporation life insurance during the year 1918, the taxable income of that corporation is abnormally swollen over and above the prewar years, not by profit, but by a loss and a loss that might seriously affect the future progress and development of that corporation; and if I understand the bill correctly, would make the proceeds received from life insurance over and above premiums paid subject to an excess or war-profit tax, depending on which one produced the greater amount of tax. (Corporations prior to 1917 were permitted to charge premiums on corporation life insurance to expense. Therefore, no corporation would be allowed to deduct over two annual premiums from the amount received in payment of a loss.)

Life insurance is devised to distribute losses. Those who live their expectancy or longer, lose on the returns from a policy or policies of life insurance if their premiums paid are computed at a reasonable rate of compound interest. Yet those who die several years prior to their life's expectancy, gain from life insurance, but most surely lose in earnings that they should have made if life had not been denied them.

It is very rare that the corporations who measure their assets in millions carry corporation life insurance. The vast majority of this form of life insurance is carried for the following reasons:

An individual interested in a corporation indorses the notes of said corporation in which he is interested. The indorser is a valuable man to the corporation, and therefore corporation life insurance is taken upon his life.

Another corporation, not so fortunate as the one cited above as to credit, may be managed well by men with ability but insufficient capital. Banks often-times require corporations in instances like this to take life insurance in making these corporations loans to protect them in event of the untimely death of the man whose only requisite to success is life.

Another corporation may in reality be nothing more than a partnership, incorporated with a third person, who is really a dummy. Yet, insurance carried on their lives is made payable to the corporation, or if they were a partnership it could be made payable to each other, and in view of the fact that they would be each other's individual beneficiary, no tax would accrue at their death from the proceeds of the policy.

Still another corporation may have in its organization a practical man in the business, another having sales ability, and still another who manages its financial affairs, either one of the three being almost invaluable to the other as a fit subject for corporation life insurance for the benefit of their firm.

I could cite you scores of other instances where corporation life insurance is almost essential to the perpetuation of a business or the protection of its credit, but without doing so I wish you to bear in mind that the perpetuation of many a man's business through corporation life insurance is as essential to the protection of his family as is a life insurance policy made payable to them as direct beneficiaries, which is free of income tax; also, how can any man's death be looked upon as being made subject to an excess-profit or war-profit tax?

Thanking you for whatever you may be able to do in correcting this inequality, I am,

Yours, very sincerely,

WARD H. HACKLEMAN.

P. S.—As a practical illustration of the point, a manufacturing concern in Indianapolis, composed of two gentlemen who control 99 per cent of the stock and an uncle of one of them, who held the other 1 per cent of the stock, secured a war contract and expanded their business. Acting upon the suggestion of their bankers, they went into the matter of corporation life insurance, and on finding that corporation life insurance as it now is, under rulings of the Treasury Department, subject to both income and excess-profits tax over and above the amount of premiums paid in, absolutely refused to buy corporation life insurance. One of them made the statement, "I'll do a great many things for my Government, but I'll not carry life insurance on my life if they want to take the most of it in tax, unless they want to pay the premiums, and I don't see any more reason why it should be taxed than proceeds from fire insurance."

The CHAIRMAN. We will hear now from Mr. Charles Johnson, representing the Publishers' Advisory Board.

STATEMENT OF MR. CHARLES JOHNSON POST, DIRECTOR PUBLISHERS' ADVISORY BOARD, 200 FIFTH AVENUE, NEW YORK CITY.

Mr. Post. Mr. Chairman and gentlemen, I shall be very brief.

I represent, Mr. Chairman and Senators, the Publishers' Advisory Board of New York, consisting of the various publishing organizations of all, or substantially all, of the periodical publications throughout the country.

The Publishers' Advisory Board consists of the Periodical Publishers' Association, the Association of Business Papers (Inc.), the Agricultural Publishers' Association, the Association of Religious Press, the American Association of Medical Publications, the Authors' League of America, and the Allied Printing Trades Council.

These publications represent an aggregate circulation of some 35,000,000 copies per issue throughout the United States, and we are here to protect not against any taxation or tax measures involved in the bill, but against the postage-zone provisions that were incorporated.

I do not wish to lay before you any rearguments or rehearings that were heard before the Ways and Means Committee at this session, but in order to conserve paper I would refer to the hearings before the Committee on Ways and Means of the House of Representatives on the proposed revenue act of 1918, part 3, beginning at page 1913 to 1950, inclusive, being the brief of the Publishers' Advisory Board, and to page 2143 and continuing therefrom, as presenting the brief of the publishing organizations.

I shall merely state that over 650 organizations, farm organizations, religious organizations, civic organizations, social and cultural organizations, including 35 universities and colleges throughout the country, have all protested against the postal-zone law.

Senator THOMAS. I notice that their protests are worded almost identically the same, which indicates that they have agreed upon a particular method of campaign?

Mr. Post. I have seen most of the resolutions, Senator. A great many are the same, and there are some that are entirely different.

I wish, in order to further spare the time of this committee, to state that I will distribute to the committee the digest of the facts and figures prepared from the hearings last year, with new matter added. At those hearings there were represented in protest against this postal-zone law the American Newspaper Publishers' Association, the Periodical Publishers' Association, the agricultural press, the Association of Business Papers, the trade union and labor press, the medical press, the religious press, country weeklies, the Southern Newspaper Association, the United Typothetae, the American Federation of Labor, the International Typographical Union, and others which appear in the digest.

I should like to present a member of the board to make a presentation on behalf of the publishers' advisory board, and I would ask that Mr. Arthur J. Baldwin be now heard, Mr. Chairman.

The CHAIRMAN. Proceed, Mr. Baldwin.

STATEMENT OF MR. ARTHUR J. BALDWIN.

Mr. BALDWIN. Gentlemen, I am a devotee of brevity---

The CHAIRMAN. I greet you!

Mr. BALDWIN. I am sure you will be as patient with me as you have been with my friend.

Senator THOMAS. You ought to be a member of the Senate.

Mr. BALDWIN. That, sir, has been a great ambition that I never dared to aspire to.

I do not purpose at this time to review the arguments in regard to this postal-zone system. You have already been very patient through the years that this problem has confronted you. I want to say this in behalf of the publishers. I have been selected to make a short statement before you to-day. It is not in the nature of an argument, but it is in the nature of a protest, or rather a statement of our attitude in order that we may be consistent upon something we think is undermining one of the great industries of this country.

There are many thoughtful men who have believed and who believe now that the zone system is wrong in principle and will result disastrously. We believe now is a dangerous time to conduct any experiments. That experiment is being conducted.

Of course, our industry was built upon a theory of our forebears that there should be in this country a principle of universal cheap postage, that a man should be able to receive his literature, his paper, his mail at one fixed rate no matter whether he lived on Euclid Avenue or whether he lived in a camp along the Santa Fe Trail. That policy has had a wonderful effect, we believe, upon the development of our country in making them one people with one language, with common aims, and has produced a morale that is standing us well to-day, and it has resulted that an American in the trenches is a "dough boy" no matter whether he was inducted into the service from the lumber regions of Michigan or whether he enlisted in New Orleans. That has been brought about in this great wide country of ours because of our national ideas, and we believe that our former condition has had a great deal to do with it.

A year ago you promised us an hour's hearing, and you gave us two days. I am going to conclude in seven minutes.

Mr. Keeler, publisher of the Chicago Herald, gave you the facts in regard to his paper and predicted disaster if the zone system went into effect. I need not remind you that the Chicago Herald has ceased publication. He based that prediction upon the fact of his wide country circulation which he could not maintain and pay this extra zone system, and he saw no way in which he could pass it on.

Senator THOMAS. He sold out, did he not?

Mr. BALDWIN. Yes, sir; that is the same thing. It ceased to be a paper, no matter whether it was sold out or not. There is so much less information, one less instrumentality of disseminating information. If we could all sell out to one paper, would that be a wise thing? That is the exact thing that is going to happen here.

I say selfishly to you, gentlemen, that so far as my own company is concerned I believe that in the long run it will result in our benefit, because there are many publishing houses that can not stand it. I believe that some great national houses—I need not mention the journals—will survive.

On that same idea Mr. Meredith appeared before you and gave you some figures in regard to the agricultural press of the company, and he predicted that a great many of them could not survive. He appeared before the House committee and gave a list of 22 publications that had ceased publication, having an annual circulation, I mean of individual copies, of more than 50,000,000 pieces of literature—they had ceased publication. Some of them ceased; some of them sold out. But whether they sold out or not, it is the same thing. There is one less instrumentality of disseminating information.

Senator GORE. That would not necessarily be true as long as they sold to some other concern.

Mr. BALDWIN. That is the way a paper ceases publication. In one instance our own concern has purchased one institution of a rival concern since the passage of the law and it has been absorbed.

Since I came into the room the gentleman handed me a little advertisement from "Printer's Ink." It is in reference to the "Sunset

Magazine" and how it has been affected by the postal-zone law. It says [reading]:

Sunset, anticipating the effect of the zone rates, long ago started out to concentrate the bulk of its circulation in the far Western States. The result has been an increase of more than 30 per cent on the Pacific slope.

At the bottom it says:

West of the Rocky Mountains, \$1.50. East of the Rocky Mountains, \$2.

That is localizing a magazine.

A representative of the New York Times before the committee said that hereafter the price of the New York Times in Texas, I believe, was to be \$19 a year.

Last week the Y. M. C. A. asked the Literary Digest for 5,100 copies of the Literary Digest for "over there." The publisher asked the Postmaster General what the rate was, and he said, "The fighting zone is in the eighth zone." The publisher notified the Y. M. C. A. that they will have to forward, in addition to the amount they send, 44 cents for each of the 5,100 subscribers. A man "over there" can not get these national magazines at the same rate as if he had stayed at home in comfort at Yonkers, N. Y. Why? Because this system is being tried out. We believe it is wrong. We believe it is an insidious attack upon one of the great fundamentals of the country.

We admit, with all the other gentlemen, even to the manufacturers of arms, that we are doing our best to help win this war; but I want to call your attention to the fact that the Government pays us nothing. We have not any arms to sell to the Government, and we do not sell the Government advertising space. We give it to them.

The publishers' attitude is this: Your problem is one of passing upon the greatest revenue bill that was ever presented to a deliberative assembly, and it is a herculean task. We do not wish in any way to hamper you in coming to a right conclusion, but we do protest against the reenactment of something that is not a revenue measure. It is an adjustment of an old postal controversy that has existed for years under the guise of a revenue act. Whatever you do, gentlemen, the press of America and the publishers pledge to you and the country our best efforts to win this war.

Senator JONES. What difference is there between your interest in this subject and those newspaper men who favored the zone system at the last session of Congress?

Mr. BALDWIN. I will tell you. Albany, N. Y., has its daily papers, but every morning the New York Times is delivered up there in the second zone as a competitor, and it goes on the news stand the same. Utica, N. Y., has its daily press, and they have a competitor. These local papers feel the competition of the larger metropolitan press.

I am talking with you frankly, gentlemen. I believe that the publisher of a paper in a city down South that sees in the advertising news that there is an appropriation of \$2,000,000 for advertising thinks that he ought to have a part of that because he publishes a paper in some small town. He can not get it. Why? Because it is for papers in national circulation, and he feels that if there is a local paper that has its dominant position and circulation in that locality a portion of that advertising revenue will come there.

There is a propaganda, an insidious propaganda, on the part of the small country papers in favor of the zone system, because it

makes them stronger in their particular locality. That is why they want to draw a line about themselves. They want to keep out Chicago papers, St. Louis papers, San Francisco papers from that particular territory, and that is the underlying reason, in my mind, of why that is.

I believe that we should have one rate, and I believe the papers that are national journals should be delivered to a citizen, no matter where he resides, so long as he is under the flag, even in the trenches, at the same rate that he would get it if he stayed at home.

That is being worked out. We are right in the throes of it. This is the first year that it has been operated, and it is an experiment that we think is dangerous, and we simply want to register our opinion that it is wrong and will result disastrously to the country.

Senator PENROSE. I would like to ask you one question. I was called out of the room during your very interesting statement, and I sympathize with some of your arguments that you present.

I am curious to know how many papers, fraternal, religious, and agricultural, have gone out of business under the zone system.

Mr. BALDWIN. Mr. Meredith gave a statement that 22 agricultural papers had ceased publication.

Senator PENROSE. I was told that; but how many others?

Mr. BALDWIN. The small papers have not gone out of business because they are exempt under the provisions of the act. The fraternal papers are exempted—

Senator PENROSE. I know, but there are hundreds, according to my recollection, of minor publications that had more or less of a national circulation, trade journals and other publications.

Mr. BALDWIN. I am not able to give you the figures. The zone system as such has only been effective since the 1st day of July. That is the reason.

Senator PENROSE. I realize that, but I would think perhaps that many of them, anticipating the consequences which they presented to us last summer, might be preparing to get out.

Mr. BALDWIN. A great many of them have sold out or have consolidated. One of the things that they face is an immense additional cost in the operation of their plant. That is a conducting cause. I am not able to give you the data on that, because I know of no source from which that could be obtained.

Senator PENROSE. I suppose the Post Office Department might have some information in it.

Mr. BALDWIN. Mr. Post, secretary of the association, tells me that from data which he has collected he understands there are about 279 that have ceased since our last hearing.

Senator NUGENT. Because of the operation of the zone system?

Mr. BALDWIN. No one can say that, Senator. I only say that the problems of the publisher are such that this is an added burden and can only help to bring about this result.

Senator PENROSE. Has it resulted in any increase in charges for advertising?

Mr. BALDWIN. It is very difficult to make a general statement like that. Many papers have increased their advertising rates because of the increase of white paper and the general costs that have gone up. Publishers have found it necessary to readjust, and they must

readjust more, because we are facing at least a 2½-cent additional rate, we understand, for the coming year.

Senator DILLINGHAM. And that goes also to the question of the subscription price?

Mr. BALDWIN. Yes, sir.

The CHAIRMAN. You have told the committee that a great many publications had ceased since this enactment. Can you give the committee a statement as to the average number of publications that have been discontinued during the three years preceding that period?

Mr. BALDWIN. Have you those figures, Mr. Post?

Mr. POST. I can send you that. That is a regular trade compilation, and I can give it to you very nearly.

The CHAIRMAN. I would like to know how many have ceased because of the act.

Mr. POST. There would be no way of making that deduction. There are papers ceasing all the time.

(Mr. Post subsequently submitted a memorandum in compliance with the request from the chairman and it is here printed in full, as follows:)

PUBLISHERS' ADVISORY BOARD,
New York City, September 23, 1918.

Hon. F. M. SIMMONS,
Senate Office Building,
Washington, D. C.

MY DEAR SENATOR SIMMONS: I am inclosing herewith a statement of the newspapers and periodicals that have ceased publication, as you requested when I appeared before the Senate Finance Committee on the 13th instant, on the protest against the "zone" law:

	Increase.					Decrease.				
	1913	1914	1915	1916	1917	1913	1914	1915	1916	1917
Daily.....	13	15	.....	20	.....	.....	.....	15	.....	.....
Triweekly.....	.....	1	3	.....	8	.....	.....	.....	2	.....
Semiweekly.....	5	13	.....	.....	.....	.....	.....	9	18	65
Weekly.....	38	57	.....	12	.....	.....	.....	224	.....	569
Fortnightly.....	10	.....	2	7	9	.....	7	.....	.....	.....
Seminmonthly.....	35	.....	.....	3	.....	.....	8	4	.....	.....
Monthly.....	37	118	70	182	1	.....	.....	.....	.....	.....
Bimonthly.....	.....	2	23	3	30	8	.....	.....	.....	.....
Quarterly.....	10	.....	19	67	31	.....	.....	.....	.....	.....
Miscellaneous.....	6	6	.....	5	5	.....	.....	.....	.....	.....
Total.....	154	212	117	299	84	8	15	252	20	629

The total increases or decreases during the years 1913, 1914, 1915, 1916, and 1917 are shown in the following table:

Year.	Sus- pended.	New.	Increase.	Decrease.
1913.....	1,428	1,574	146	.....
1914.....	1,491	1,698	197	.....
1915.....	1,547	1,412	.....	135
1916.....	1,327	1,545	279	.....
1917.....	1,650	1,043	.....	616

You will observe from this table that in the year 1916 the increase in periodicals was net 279, and of these the large majority were issued as weeklies and monthlies, i. e., publications issued less often than weekly, in other words, periodicals of a national appeal as distinguished from newspapers of local character.

Mr. BALDWIN. I would like to file as a part of the record a memorial that was signed by the editors of some 40 national journals in which they record their objections to this plan and reasons from an economic standpoint.

The CHAIRMAN. Just hand it to the clerk, please.

(The memorial referred to above is here printed in full, as follows:)

MEMORIAL TO THE CONGRESS OF THE UNITED STATES FROM THE EDITORS OF THE
PRINCIPAL AMERICAN PERIODICALS.

The periodical press of the United States is the national circulating library of the people. Books are counted by the thousands; periodicals by the hundreds of thousands.

The aggregate circulation of the popular magazines in America is undoubtedly sufficient to put one magazine—possibly two—in every American home, and the visitor rarely goes to any home in America, except in the most congested districts of a few of our great cities, without finding on the table one or more magazines.

Among these periodicals are special publications edited by specialists and containing expert information for the members of every vocation in life.

There are special periodical publications for the lawyer, the doctor, the minister, the engineer, the manufacturer, the farmer, the banker, the merchant, the artist, and the housekeeper.

These periodicals are essential to enable the men and women in these various locations to keep up with the demands of their time. They are registers of professional practice, they report the theories, the experiments, the successes, and the failures of the pioneers. They report these facts months and sometimes years in advance of their report in books and encyclopedias. They are one of the secrets of the progressive spirit of the American people. Coupled with the facile and alert mind of Americans, they make sane progress possible.

These special publications are necessarily limited in their circulation by the vocations to which they severally belong. But there is no limitation to the circulation of the popular monthly and weekly periodicals. To them the best writers of America and England contribute. In them are found the best fiction. They furnish recreation, inspiration, idealism to millions of readers.

But these periodicals do much more than this. They deal with every department of knowledge. They interpret the works of the great thinkers in terms understandable by nonexpert readers. Just now they are giving the public, to an extraordinary degree and with extraordinary excellence of quality, articles descriptive of the war and articles interpreting the new duties which the great world war imposes on the American people. These articles are read with a care which is not often given to publications in the daily press, are passed from hand to hand, are the subject of discussion in homes and clubs, and exert an inestimable influence by inciting men to think and by guiding their thoughts in right channels.

But the war does not absorb the attention of either the contributors to or the editors of the periodical press.

Take up a pile of periodicals for the last two or three months lying on the table of any library or club. You will find in them articles written by authors possessing special information describing public leaders; an analysis by those who know of the conditions in Russia which interprets and enables us to understand the extraordinary events in the recent history of that enigmatical country; trustworthy accounts of what our own people are doing in food control and food production; pictures of travel, which give the reader that breadth of view absolutely necessary to prevent a narrow provincialism and to equip

the Nation with that international understanding essential to any hope of eventual international peace; and articles by experts on health and the home, telling the fathers and mothers how to preserve the health of their children and how to protect the home.

This periodical press, circulating nationally and made by the post office available, not only to every town and village, but to every rural resident within reach of the almost omnipresent post office, dissolves provincial prejudices, enables the North to understand the South and the South the North, the East to understand the West and the West the East. It unifies and nationalizes. It equips the people of all sections with the same knowledge and inspires them with the same ideals.

It dissolves sectarian and class prejudice. It teaches a practical religion useful to men of all creeds because not written in the interest of any creed. It discusses ethical and spiritual theories with the freedom to which the church of the past has generally been a stranger.

It describes the great industrial operations and discusses the great industrial problems from every point of view.

In this periodical circulating library the theories of the labor unionist, the socialist, the capitalist, are all represented and the doctrines of each class get a hearing from the apostles of the other classes.

It thus ministers to an extent too little appreciated, not only to the interest and intelligence of all the people, not only to the progress of the people as a whole, but to that mutual understanding and that common patriotism which are essential to a united and an efficient Nation.

These periodicals are without exception sold to their subscribers for less than cost. There is probably not a periodical in the country which does not pay to its editors, its contributors, its compositors, its pressmen, and its office workers and the paper makers more than it receives from its subscribers.

What enables it to do this is the income derived from the advertisers. Pupils almost never pay for their own education. The State support the public schools; endowments support the colleges and universities; the advertising supports the periodical press.

This advertising makes of the whole country a great perpetual, but ever-changing, national fair. It brings before the eyes and mind of the American people the products of American skill, enterprise, and energy.

It nationalizes trades, standardizes goods, makes it possible to produce them on a large scale.

Modern automobiles, modern breakfast foods, modern cheap watches, would have been impossible if the periodical press had not created this nation-wide market.

It promotes healthful competition and stimulates the competitors both to improve the quality and lower the prices of their products.

It promotes a habit of national integrity because it brings the Nation's goods into the public light and into a public competition.

It has driven the peddler with his cheap goods and his shoddy and sometimes fraudulent imitations out of business.

The four corner stones of the Republic are the free church, the free school, the free press, and the free assembly. Open attack upon any of these corner stones is scarcely possible. The Nation would take instant alarm. But insidious attacks undermining one or all of them is possible. Against such insidious attacks the Nation needs to be on guard.

Without these corner stones of the Republic free elections would be an idle form. Free elections interpret the national intelligence and declare the national will. A free church, a free school, a free press, and a free assembly, maintained by the people, all of them springing from the people and all of them pervading the Nation from the Lakes to the Gulf and from the Atlantic Ocean to the Pacific Ocean, are essential to develop national intelligence and create a national will. Without them there would be no national intelligence

to discuss and no national will to decide the great issues which confront democracy.

Lyman Abbott, editor the Outlook; Wm. S. Woods, editor Literary Digest; Geo. H. Sandison, editor Christian Herald; John M. Siddall, editor American Magazine; Frank Crowninshield, editor Vanity Fair; Bruce Barton, editor Every Week; Albert Shaw, editor Review of Reviews; John A. Sletcher, editor Leslie's Weekly; Griffith Ogden Ellis, editor American Boy; Charles F. Jenkins, editor Farm Journal; Edgar Sisson, editor Cosmopolitan; Harry A. Thompson, editor Country Gentleman; H. T. Whigham, editor Metropolitan Magazine; Myra G. Reed, editor McCall's Magazine; Geo. E. Cook, editor The Mother's Magazine; Geo. W. Larimer, editor Saturday Evening Post; I. A. Waldron, editor Judge; Arthur Hornblow, editor The Theater; Edna Woolman Chase, editor Vogue; Richardson Wright, editor House and Garden; Moody B. Gates, editor People's Home Journal; J. A. Mitchell, editor Life; Harford W. H. Powel, jr., editor Harper's Bazaar; Edward Bok, editor Ladies' Home Journal; Charles W. Burkett, editor American Agriculturist; Douglas Z. Doty, editor Century Magazine; Isalah C. Parrott, editor Modern Priscilla; C. F. Chapman, editor Motor Boating; Altamont Vance, editor Pictorial Review; Charles K. Field, editor Sunset Magazine; Hiram Moe Greene, editor Woman's World; Sarah Field Splint, editor To-day's Housewife; Gertrude B. Lane, editor Woman's Home Companion; C. G. Sinsabaugh, editor Motor; Frederick L. Collins, editor McClure's Magazine and Ladies' World; W. F. Bigelow, editor Good Housekeeping; W. Sammons, editor System; Nolan R. Best, editor Continent; Edward J. Wheeler, editor Current Opinion; Hamilton Holt, editor Independent.

The CHAIRMAN. Mr. Francis F. McIlhenny is present and desires to be heard. You may begin now, Mr. McIlhenny.

STATEMENT OF MR. FRANCIS F. McILHENNY.

Mr. McILHENNY. Mr. Chairman, I will only take probably about half the time taken by the last speaker.

This morning you heard from the oil producers. I represent a company which is both a producer and a refiner of oils, and our problem as regards this revenue law is slightly different. The Sun Co., of Philadelphia, does both a production and a refining business; and so far as the production part is concerned I would merely affirm what was said by the gentleman this morning. As to the refining part I would, with your permission, call your attention to one clause of the bill.

This bill provides in the income section—

Senator THOMAS. What page?

Mr. McILHENNY. Page 37—that corporations can amortize their buildings, machinery, equipment, and facilities which they purchased after we entered the war. There is a check on that amortization that within three years after the end of the war the Commissioner of Internal Revenue can go over the books of the corporation and if it has been amortized too much he can collect the tax which should have been paid.

An oil company which is in the business of refining of oil must carry a large stock of oil at all times. There is quite a little period between the time the oil comes out of the ground and the time when the oil company can put it into the hands of the consumer. The result is that oil companies who are doing a refining business, whether

they get their oil by production or by purchase—and the company which I represent does about 50 per cent of each; that is, it buys about half of its oil and produces the other half—it must keep on hand a large supply of this crude oil in order to meet the transportation and the time that has elapsed between the time they get it out of the ground and into the refinery to refine it.

I would say that, roughly speaking, oil companies would carry in refined and unrefined stocks of oil at least 25 per cent of their invested capital. In other words, if an oil company has \$30,000,000 of invested capital, it would have to have about \$8,000,000 at all times invested in refined oils and crude oils.

If they want to keep up their production of refined oils, they must keep up that much of a stock of crude, because if they do not they will not have enough oil at all times to keep the refinery supplied.

The result is that he buys that crude oil, under present conditions, at high prices.

A large part of the business of the Sun Co. comes from Texas crude oil. I should say that since 1915 the cost of Texas crude oil has been an advance of about 50 per cent a year. In 1915 the price of Texas oil was about \$1 a barrel. It had been down as low as 60 cents within a very brief period before then. The price is now about \$2 a barrel. In other words, the refiner every year has got to find 50 per cent more capital so he can maintain the same quantity or number of barrels of crude oil.

The result is, the way this scale is drawn, that unless he can amortize those higher priced stocks that he has been buying since the war began he will not have enough money to keep up his stock of crude oil, because it requires additional capital each year, because the price is going up and will go up to the end of the war in order to maintain the same amount of stock—

Senator SMOOT. That is the case with every business in the United States.

Mr. McILHENNY. I think it is, Senator, probably more in the case of the company I represent because we probably have a little larger percentage of our total investment in raw materials.

Senator SMOOT. A merchant has got to carry the whole stock.

Mr. McILHENNY. I think a department store would have to do perhaps more.

Senator SMOOT. Everything he has got.

Mr. McILHENNY. The storekeeper would have more than any of us.

Senator SMOOT. Generally more than his capital stock.

Mr. McILHENNY. I should think so.

So, what we ask you to do in this bill is this. We can not keep up our production of oil which the Government needs. The Sun Co.'s business is almost altogether a lubricating oil business. A large percentage goes to France and Italy and England, and to the manufacturers of munitions, because it is used in lubricating the machinery which is used in manufacturing munitions. We can not keep up our production of refined oil unless we can amortize our crude stock.

Senator JONES. It was stated by one oil representative this morning that the war had practically reduced the demand for oil, and when the war is over there will probably be an expansion of the demand. I suppose the price will go up to \$3 a barrel after the war?

Mr. McILHENNY. I did not perhaps understand him this morning to say that the demand for oil——

Senator JONES. He said the demand was increasing everywhere.

Mr. McILHENNY. Oh. The demand is increasing?

Senator JONES. Yes.

Mr. McILHENNY. Well, I suppose that is so, normally. Whether the demand after this war is over for lubricating oils will be as great as it is now I am not prepared to say. I would think it would be less.

Senator JONES. Are you willing for the Government to go into partnership with you and take "pot luck" with you after the war?

Mr. McILHENNY. We would be willing to take chances with the Government that the price of lubricating oils will drop after the war. I feel very sure, Senator, that the price of lubricating oils will decrease after the war is over.

The CHAIRMAN. It is true that everybody who buys at the present prices, if there should be a sudden slump after the war closes——

Senator JONES. What has become of that \$8,000,000 worth of oil that you bought at a low price and kept on hand?

Mr. McILHENNY. The amount we got at a low price we made a substantial profit on. We have to replace that with higher-priced oil, so that the reservoir is always kept full. So in time you gradually raise the average price of your oil.

Senator JONES. How do you figure it, when you still have got your pipe lines filled with that low-priced oil, and instead of making a profit, just figure it that way——

Mr. McILHENNY. Of course, Senator, that low-priced oil was in the refined stocks. Those refined stocks closely follow the value of the crude oil.

Senator GORE. The price of the refined product is relative to the price of the crude.

Mr. McILHENNY. Yes, sir. And as we buy higher-priced crude that price goes up and you gradually raise the average price of it.

Senator JONES. Have you not made considerable profit by reason of the advance in the price of oil?

Mr. McILHENNY. The company has done well. Whether it has been that or not, I do not know.

The company I represent, like so many others in America, is owned by a few people, and we have never had a very large amount of capital stock issued. Practically all our earnings in 1918 will be under the 80 per cent clause. We had very small earnings in 1911, 1912, and 1913. A great part of the actual business done by the company in those years will be subject to the 80 per cent tax, and that is the objection I have to the bill. We do not mind paying the tax, provided enough money is left us to finance the increased cost of our raw materials by amortization. If that is too much, the Government has a check on this after the war, within three years, to go over that tax, and if it has not dropped that much by reason of the end of the war the Government gets the extra tax. We do not get any more profit one way or the other, but we will have enough money, if you amortize these stocks, to conduct our business.

In other words, there is no difference between a building and supplies. The act gives you the right to amortize your building bought

at higher prices, and you ought to have a right to amortize the supplies.

Senator PENROSE. Have you prepared an amendment?

Mr. McILHENNY. I will just put in the word "supplies" in addition to the word "machinery"—

Senator PENROSE. I think it would be well to dictate to the stenographer just where and how you want the bill amended.

Mr. McILHENNY. Amend section 234, subdivision 8, in line 20, by inserting, after the word "machinery," the words "material, supplies."

Senator, has anybody discussed the question of inadmissible assets at this meeting?

The CHAIRMAN. No, sir.

Mr. McILHENNY. The Sun Co. conducts its business largely through subsidiaries. In other words, this company, which is all one business, has found it convenient and easier to comply with State laws. For instance, if it wanted to go into the production field in Oklahoma it found it better to take out an Oklahoma charter for its Oklahoma business; or if it wanted to go into Kentucky, to take out a Kentucky charter, etc. So these companies have gradually got to owning a lot of subsidiary companies.

On page 60 of the bill it provides for inadmissible assets, and what I speak of as to the Sun Co. applies to every corporation in America which owns subsidiary or affiliated corporations.

The parent corporation, when it gets its dividends from the subsidiary, does not have to have any income tax on the dividend. And so the bill, on page 60, says that in figuring up this invested capital for the profits tax the parent corporation can not include in its invested capital the stock of those companies from which it gets its dividends.

On page 62 it says that when you come to figure up your invested capital and you deduct the amount you have invested in these subsidiaries—for instance, if the corporation is a million-dollar corporation and has a hundred thousand dollars invested in a subsidiary, you take the \$100,000 for your million dollars and you have \$900,000 left as invested capital.

In 1917, under the rulings of the commissioner, if you had borrowed money, you could offset the money borrowed against these stocks you own. In other words, if a group of men took a million dollars and formed a corporation, they took a hundred thousand dollars of that money and they put it into stock of the subsidiary. Then they go to the bank and they borrow another \$100,000, so that they have, all together, a million one hundred thousand dollars to use.

Last year the commissioner ruled that in such cases as that it would not be fair to make a man deduct his liability of a hundred thousand dollars he borrowed from the bank and also money he had invested in the subsidiary. So the commissioner last year let him offset one against the other, and deduct \$100,000, leaving him a capital on which he would get a deduction of \$900,000—

The CHAIRMAN. Assuming that the \$100,000 that he borrowed was invested in the subsidiary?

Mr. McILHENNY. Yes; but, of course, you can not trace it. It is always invested in a subsidiary, because you have a certain amount

of money, and if you do not use it for one thing you use it for another.

On page 62 of this present bill it says that you must take both. In other words, you have got to deduct from your invested capital not only the money you put in your subsidiary, but the amount of money you borrowed from the bank. In other words, instead of having \$900,000, the Government only lets you have the benefit of an invested capital of \$800,000.

That is a rather complicated and technical thing, but it is a very real and important thing to corporations which must do their business throughout the whole country as against corporations localized in one State; and a corporation like the Sun Co., whose subsidiaries are not in competition, but just to comply with the various State laws throughout the country they have found it convenient—

Senator THOMAS. The subsidiary company in the case you mention would be entitled to its \$100,000, would it not?

Mr. McILHENNY. Yes; it gets a deduction—

Senator THOMAS. So that really the parent company does not loan that \$100,000?

Mr. McILHENNY. No, sir; that subsidiary pays tax to the other.

Senator THOMAS. I understand it does.

Mr. McILHENNY. It pays tax as well, and the Government gets the tax on the money that that subsidiary earns; and there is no reason why it should get the tax on the \$100,000 that it borrowed from the bank.

Senator THOMAS. That is another proposition.

Mr. McILHENNY. All we ask is that the law as it was interpreted last year be continued this year; that is to say, that you can not deduct generally; you can not have the subsidiary counted as being an admissible asset; but if you have borrowed money, you can offset one against the other, because the Government gets its tax if you borrow the money just the same. The money is in use just the same.

Senator THOMAS. I do not see any distinction between allowing capital which is owned and disallowing capital which is borrowed, provided it is used in the business. If you have \$100,000 to go into business and I borrow another \$100,000 and go into the same business, you would be allowed your \$100,000, and I will not be allowed my \$100,000 that I borrowed, although that is my capital.

Mr. McILHENNY. If you take your \$100,000 and put it into corporation stock, you have not got \$100,000. You have nothing invested at all. You have borrowed it all. You are allowed nothing, because you offset the \$100,000 you borrowed against the \$100,000 in stock.

If you have \$300,000, this bill would make you deduct the \$100,000 you put into this subsidiary.

I will not take your time further, because the hour is late.

There is one other thing that I would like to present as representing companies which are conducted through allied or subsidiary companies.

Last year we were allowed to file consolidated returns. This bill specifically says that consolidated returns shall not be allowed. That is a great inconvenience to a corporation running its business with subsidiaries, not to be allowed to file consolidated returns.

Senator SMOOT. It is a great deal better for the Government.

Mr. McILHENNY. To file them separately?

Senator SMOOT. Yes.

Mr. McILHENNY. The Government would get more taxes; yes.

Senator SMOOT. That is the object of the bill.

Mr. McILHENNY. It makes the tax fall unfairly upon some particular company in the group.

Senator SMOOT. They have subsidiary companies; and if one loses, it would be given credit for it; and if it gains——

Mr. McILHENNY. If this parent corporation had taken all its money and invested it in plants, in property, instead of subsidiary corporations, it would file a consolidated return.

Senator SMOOT. Take a newspaper that in one or two of the large cities of the United States is making a great amount of money. That same newspaper may be running papers in different cities in the United States and every one of them be losing money. The successful companies would be compelled to pay a higher rate of taxation; but if they are allowed to deduct the losses that they are sustaining in other cities, their tax would be nothing in the city in which they are making large profits.

Mr. McILHENNY. Of course, if those seven or eight newspapers were all owned by the same individual, he could deduct the loss. Unless they are separate corporations——

Senator SMOOT. They can deduct the losses of that company in that particular city. It is not owned by the parent company, but owned by the same individual.

Mr. McILHENNY. A mercantile business such as this oil company is conducting find that they can obey the law better in this way——

Senator SMOOT. Your subsidiary companies are organized under the laws of the different States?

Mr. McILHENNY. Yes, sir.

Senator SMOOT. A different corporation?

Mr. McILHENNY. It is all the same business. The business is run as an entirety.

I think, Senator, that I have nothing further. I hope very much that you will amortize the supplies of business, because I think when the war ends that there will be a very difficult period of adjustment otherwise.

(A statement was submitted by Mr. McIlhenny, and is here printed in full, as follows:)

PHILADELPHIA, PA., September 11, 1918.

HON. FURNIFOLD McL. SIMMONS,
United States Senate, Washington, D. C.

DEAR SIR: We beg to send you this letter giving some reasons why the proposed revenue bill should be modified.

We assume that the first and most sacred task of the American people is to win this war decisively and quickly, and therefore an adequate supply of money must be provided; that this money, so far as practicable, should be raised by taxation, and that business should not receive extortionate profits as a result of war work.

But there is a limit beyond which taxation defeats its own purposes. The limit of taxation on business doing war work must be fixed by four factors: (1) Maintenance of production; (2) maintenance of credit; (3) avoidance of bankruptcy now or following the war; and (4) fairness to the owners of the business.

It is submitted that the taxation in the proposed revenue bill exceeds all four of these factors.

Maintenance of production.—With the soaring costs of everything that goes into manufacture, additional capital must be constantly added; this is so even

If production is not increased. Sufficient new capital can not now be obtained from outside sources. Money can be borrowed from the banks only with the greatest difficulty, and to float loans with the public is out of the question. Additional funds must come from earnings, and the small amount of earnings which the proposed bill permits business to retain is not sufficient. If the bill is passed in its present form a curtailment of the production of necessary war materials must necessarily follow. The oil business is a fair example of this proposition. Every oil company must carry a large supply of crude and finished oils in addition to all of the other supplies it requires. No manufacturer carries more raw and manufactured materials and supplies than he needs, and any decrease in these supplies carried means a decrease in production. Crude oil and its products have been increasing in cost 50 per cent per year since the beginning of the war. Even without speeding up production, additional capital invested in these raw materials must be increased 50 per cent. This equally applies to other manufacturers, to department stores, and other lines of business. To meet this a sufficient margin of earnings over taxes must be allowed.

Maintenance of credit.—Business must constantly get some credit on short-time loans from banks, but present conditions render it impossible to procure large credits, and, even if business could get large loans, it is not safe now to become heavily extended. That is to say, safety requires that business should be allowed to maintain its production out of earnings instead of impairing its credit by loans, even if they could be obtained.

Avoidance of bankruptcy.—If sufficient earnings are not allowed to the business, it will either be compelled to decrease production or attempt to extend its credit beyond safe limits. This will lead to bankruptcy in some cases before the end of the war. If business is to avoid financial strain after the war, when prices drop, it should be allowed to accumulate a sufficient reserve to stand the heavy losses which will be entailed in the shrinkage of the value of its supplies. For example, say a grade of crude oil is now purchased for \$2 per barrel (and there will be an increase rather than a decrease as the war goes on), when the war ends, if the price of this oil drops to normal, say \$1 per barrel, the oil company on every \$2,000,000 now invested in oil stocks will have a positive and direct loss of \$1,000. The law allows no compensation for this.

Fairness.—It is not proper, either for the national welfare or in fairness to the corporation, to compel it to carry on its books its high-priced materials at war prices, and to stand the loss when the prices drop. The proposed law permits amortization of buildings erected at war prices (sec. 234, par. 8), and it should permit amortization of all sorts of supplies bought at war prices. There is no argument which applies to buildings which does not apply to supplies, as these supplies are in fact a part of the investment, for without them a business can not be operated. For example, an oil company (and other business on the same basis) must have a large part of its invested capital in raw and finished products. An oil company with \$10,000,000 of capital will have on the average, say, between \$2,000,000 and \$3,000,000 invested in oil stocks. As the cost of these oil stocks increases at 50 per cent a year, as has been the case since 1915, the excess cost of these stocks would exceed the net profits allowed under the proposed law. Therefore, at the end of the war the loss by reason of shrinkage of value would exceed the profits allowed under the bill. Unless oil stocks may be amortized, most oil companies, from a financial standpoint, would be better off to discontinue their business until after the war and get rid of their high-priced raw materials, and so avoid the inevitable losses which must follow when these prices drop to normal.

The remedy for the foregoing objections to the bill.—A large part of the injustice of the bill as above outlined could be avoided by amending the bill to permit amortization of raw and manufactured materials on hand, supplies, and equipment in the same way as amortization is permitted in the case of buildings under section 234, subdivision 8. This amortization would eliminate fictitious earnings on the books and would allow a reserve fund necessary to meet the increased demand for new capital and the loss which will follow when prices drop to normal. If the bill is not amended in this way, business must curtail its supplies on hand and, as a result, its production. As an officer of a corporation, I must protest most vigorously against the above feature of this proposed bill, which would make the corporation keep its books so as to show fictitious profits.

Some other objections to the bill.—Section 326, subdivision 5 (c), stipulates that invested capital does not include money borrowed and payable within a

year or capital invested in so-called inadmissible assets. It does seem, however, that should a company have a large bonded indebtedness maturing over a period other than one year, this bonded indebtedness may offset the inadmissible assets. If, however, a company pursuing its regular form of financing has renewed its obligations from year to year, they are penalized for so doing. Such a provision as this, which precludes the possibility of offsetting inadmissible assets with short-term indebtedness, accounts payable, and current liabilities, is indefensible. As an illustration, a corporation may according to its practice borrow a million dollars from the bank on short-time obligations. That same corporation may use this money to finance a subsidiary corporation. By so doing the company would have to deduct \$2,000,000 from its invested capital, or a net loss of \$1,000,000 in invested capital due to the transaction, whereas the corporation, according to the best bookkeeping practice, has not added to or taken from its net worth. By such a process it is quite impossible that a large corporation of great net worth might have, according to this new law, its invested capital reduced to nothing or less than nothing. There is no sound reason why a corporation should not borrow money and invest this money in a subsidiary corporation. All large businesses, such as an oil business, which must conduct its affairs in a number of States in order to comply with the law of those States, have been compelled to take out new charters, although the business is run as an entirety. These subsidiary companies conduct different operations and do not lessen competition. For example, an oil company often does oil production work in one State under one charter and in another under a charter from that State. In 1917 business was allowed to offset borrowed money against these stocks in subsidiaries, and this should still be permitted.

Consolidated returns.—In 1917 consolidated returns were permitted in the case of a corporation and its subsidiaries where 95 per cent of the stock ownership was identical. The reasons for permitting consolidated returns are too self-evident to justify taking up space in this letter. •

Amortization of equipment.—In section 234, subdivision 8, amortization is allowed on buildings, equipment, and facilities acquired after April 6, 1917. Without doubt this applies or should apply to the cost of oil wells. Section 9, however, makes this provision somewhat confusing. The wording should be changed in section 9 or entire clause left out.

Average income of prewar years.—A company should be permitted to earn on its present invested capital the same rate of interest as it earned on its then invested capital in prewar years. The plan in the proposed bill puts a premium on a business which has a large invested capital as against the business with a small invested capital and superior energy, industry, and ability in its management.

Contributions.—Most corporations have given liberally to the Red Cross and other charitable organizations. An enactment of this law will make further contributions of this character impossible. We had hoped—and it surely would be proper—that a provision would be inserted in this law permitting an exemption from net income of all contributions made.

In conclusion.—If corporations in this country are to avert disaster this bill must be amended so that the books of the corporations can be kept without showing fictitious profits and so that the rate of tax will be low enough to let the corporation finance the increased cost of supplies and to prepare for the losses which will inevitably accompany the decrease in prices following the war.

Respectfully submitted.

SUN Co.,
Per FRANCIS S. MCILHENNY,
Vice President.

The CHAIRMAN. We will now hear from Mr. D. J. Tompkins.

STATEMENT OF MR. D. J. TOMPKINS.

Mr. TOMPKINS. I will consume but about five minutes; perhaps less.

The revenue act of October, 1917, imposes a tax of 1 per cent on the premiums written by insurance companies—fire, marine, casualty, and all others; life insurance, of course, although life is a little different. It includes also fidelity and surety companies.

I represent these fidelity and surety companies. I am president of one of them. The tax is all right. The bill permitted the fire, marine, and casualty companies to make a monthly report to the Internal Revenue Department of the premiums written and pay the tax of 1 per cent on the amount stated in the report. That was easy. The department got their money monthly, and it was quite satisfactory. The fidelity and surety companies were treated very differently in the bill. They were subjected to a stamp tax. That is an easy way of getting the tax, yes; but it is a very troublesome way to the companies. We not only have to affix the stamps and cancel them, but indorse upon each bond or policy a certificate as to the amount of the premium charged and the rate charged, so that the obligee receiving the bond can know that the law has been complied with as to the stamp being affixed for the amount of the premium. These bonds often are executed in duplicate. The duplicate has to have an indorsement put upon it to the effect that the affixed stamp has been affixed for the rate of premium upon the original.

There is another thing. All those things involve a large amount of clerical work. They keep from one to three clerks busy in every fidelity and surety company's office. Oftentimes the tax is pretty nearly as much as the premium when they are written for a short term. The fidelity and surety companies think that it is hardly fair to put upon them the burden of affixing these stamps, when the fire, marine, and casualty companies can make the monthly report.

These monthly reports, like the form I have here, have got to tally if the internal-revenue commissioner checks them up with the annual reports. They have got to tally. They have got to be right. The Government is not losing money in that operation, and it is very much more simple so far as the companies are concerned.

There are always quite a proportion, maybe 2 to 5 per cent of the policies, that are not taken. We affix a stamp on them. The obligee consults his attorney and the attorney says, "We want some provisions in this changed." That stamp is wasted. We have got to write a new bond and execute it over again and pay another tax. There are a good many of those instances.

Recently, in writing bonds required under the Railroad Administration's regulations from shippers and consignees in respect to freight charges, I guess fully one-third to one-half of the bonds that we have written since the 1st of August have come back to us for reissue, because it was decided by somebody that they wanted different roads included under the bond, one or more, 1 or 5 or 10. So we had to execute them over again.

Senator GORE. Have you any idea what the stamps would aggregate on that bunch of bonds?

Mr. TOMPKINS. The stamps would be only from 5 cents to 20 cents.

Senator GORE. I mean the aggregate amount.

Mr. TOMPKINS. Oh, the aggregate. The aggregate would probably be \$30 or more.

In many instances we prefer to forego the stamps, lose them, rather than to take the trouble to collate them and go to the internal-revenue collector's office and get them redeemed. It is a great bother.

Now, you might say that as far as all that goes you do not care very much about it. But if the fidelity and surety companies were taken

out of the stamp section and put into the monthly report section, like fire, life, and casualty companies, the Government would get a good deal more revenue by it, because there are not less than five—probably seven and a half or maybe nearer ten millions—of premiums written annually on which the Government now loses the tax. Why? Because they are on bonds issued to States, municipalities, counties, and public bodies, which bonds, under the decision of the Supreme Court in the Ambrozini case and under the rulings of the internal-revenue commissioner are held to be nontaxable so far as documentary stamps are concerned that it is an interference with the governmental functions of those bodies for Congress to attempt to make those obligations subject to a stamp tax. Therefore they have to go free.

Senator GORE. When was that case decided?

Mr. TOMPKINS. I do not know just what year, Senator, but it is 167 United States Reports, page 1.

Senator ROBINSON. Have you discussed with the Commissioner of Internal Revenue the advisability of putting your companies in the class that make monthly reports?

Mr. TOMPKINS. I will come to that, Senator—

Senator THOMAS. What is the name of that case that you mentioned?

Mr. TOMPKINS. Ambrozini against the United States, 167 United States, page 1.

Those premiums on bonds issued to States and municipalities are oftentimes large. The bonds for public officials are large and the premiums are large. The aggregate of those premiums is quite large.

Senator LODGE. If you were just charged a tax on the premium of those bonds and report it each month, that tax would be constitutional and you would pay it—

Mr. TOMPKINS. That tax would be all right. It forms a part of the amount on which the company pays the income tax. There is no objection to that.

Senator LODGE. If it were collected in that way it would take it out of the objection?

Mr. TOMPKINS. Yes, sir. It would be paid as a premium tax. We are not objecting to the tax at all.

Senator LODGE. Does the department object to this?

Mr. TOMPKINS. I do not think it does. I wrote on June 4 to the chairman of the Senate Finance Committee, Mr. Simmons, a letter inclosing a brief, a copy of which I have here, suggesting changes. I sent a copy of that letter to the Internal Revenue Commissioner, Mr. Roper, who replied on June 11 [reading]:

Permit me to thank you for your very interesting and suggestive letter of June 4, 1918. It will be carefully studied and considered in connection with any recommendations which I may be called upon to make regarding new tax requirements.

Senator ROBINSON. What is the date of that letter?

Mr. TOMPKINS. June 11, 1918. I went to the commissioner's office this morning and was told that he was so busy that he could not see me to-day.

Senator ROBINSON. I can not see any reason, now, why it should not be done. It seems to me it would simplify the matter.

Senator LODGE. I think so.

Senator THOMAS. Suppose you file that statement.

Mr. TOMPKINS. I did not expect to bother this committee with the larger matters. I did not expect to appear before you to-day.

The CHAIRMAN. We will send that letter to the commissioner with the request that he present to the committee any views he may have in respect to the letter.

Mr. TOMPKINS. The Commissioner of Internal Revenue?

Senator PENROSE. The chairman means that the committee will send it.

Mr. TOMPKINS. I did not expect to appear here at all, because I thought it was not important enough to take up your time with. I addressed a letter to you this afternoon and left it in your office, referring to this letter and inclosing Commissioner Roper's letter.

I thank you.

The CHAIRMAN. The committee will stand adjourned until to-morrow morning at 11 o'clock.

(Thereupon, at 5.30 o'clock p. m., the committee adjourned, to meet at 11 o'clock a. m. to-morrow, Saturday, September 14, 1918.)

TO PROVIDE REVENUE FOR WAR PURPOSES.

SATURDAY, SEPTEMBER 14, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 11 o'clock a. m. in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present: Senators Simmons (chairman), Thomas, Robinson, Gore, Jones, Gerry, Nugent, Penrose, Lodge, Smoot, Dillingham, and Townsend.

The committee resumed the consideration of the bill (H. R. 12863) "to provide revenue, and for other purposes."

The CHAIRMAN. We will hear first this morning Mr. R. J. Hamilton.

INCOME TAX.

STATEMENT OF MR. R. J. HAMILTON, SECRETARY OF THE AMERICAN RADIATOR CO., WASHINGTON, D. C.

Mr. HAMILTON. Mr. Chairman, my name is R. J. Hamilton, of Chicago, temporarily residing at Washington.

Senator NUGENT. What interest do you represent?

Mr. HAMILTON. I represent, as secretary, the American Radiator Co., and am here to present two features of the income-tax and excess-profit tax provisions which have appealed to us as being subjects of public interest, and not so specifically of a special interest to ourselves.

The first feature I had in mind—and very informally, because I did not know until 10 minutes ago that I was going to be heard—is one which concerns our company specifically, in common with many others, and it has to do with the situation of companies who have built up organizations and businesses in foreign countries. Our company introduced steam and hot-water heating—modern heating—in the entire Continent of Europe, and during a period of over 20 years have built up a large organization, with factories and selling organizations in the various countries of Europe, at the moment through the war being confined to the countries of England, France, and Italy, in each of which we have factories and selling organizations, as we also have in Canada, and I take it that what I say will be more applicable to Canada, as regards the number of concerns affected, than it will be to Europe, though in our case the European situation predominates.

Senator SMOOT. There are hundreds of institutions similarly situated in Europe.

Mr. HAMILTON. Yes; I assume so, and perhaps a thousand in Canada.

The CHAIRMAN. I understand you to say that you not only sell in Canada and these European countries, but you have factories there?

Mr. HAMILTON. We have factories in each of these countries.

The CHAIRMAN. And you have factories in this country?

Mr. HAMILTON. And factories in this country.

The CHAIRMAN. Do you sell in those countries the goods that you produce in this country?

Mr. HAMILTON. No, indeed; only the goods that are produced in those countries. We started in Europe, as I said, over 20 years ago, with a mere nest egg, a moderate financial investment. Until the current year there have been no dividends paid on that investment. It has accumulated until an original investment of slightly over a million dollars has grown to an investment to-day of approximately \$10,000,000. This year, having attained a certain prosperity over there through these years of conservation of our assets, etc., we are in a position to pay fairly generous dividends to the parent company, the home company, the American Radiator Co.

Senator SMOOT. Are you making munitions of war over there?

Mr. HAMILTON. We are making munitions of war in England, France, and Italy on a very generous scale.

The CHAIRMAN. They are separate corporations?

Mr. HAMILTON. They are separate corporations, each under the laws of the country in which it is organized.

Senator SMOOT. Subsidiary companies?

Mr. HAMILTON. A hundred per cent of the stock of each one is owned by the American Radiator Co., a New Jersey corporation.

Those companies have already actually transmitted to us, during the year 1918, a sum in excess of \$500,000 as dividends, and are in a position to increase that amount this year, and, in so far as we can see, barring the exigencies we can not foresee, of course, they are in a position to continue dividend payments in the future.

Senator NUGENT. Are those dividends derived from the manufacture of munitions or the manufacture of radiators?

Mr. HAMILTON. Both, Senator.

Senator NUGENT. Can you segregate them?

Mr. HAMILTON. We can segregate them perfectly. I might say, however, lest our situation appear in a false light, we are not making any more money making munitions this year or last year than we were making in our more prosperous days in the manufacture of boilers and radiators alone. There is no question of profiteering in the manufacture of munitions.

Senator NUGENT. Are you manufacturing munitions under contract with the American Government or with the foreign governments?

Mr. HAMILTON. Under contract with the respective foreign governments of the countries in which the factories are located.

As regards these dividends that have been transmitted to us, and may be transmitted to us unless we find it necessary to stop the flow, we find no compensating element whatsoever in the present income and excess-profits tax bill. In England, France, and Italy each country has an excess-profits-tax law which, although quite more

generous in its exemptions than the law proposed in this country now—and that is literally true—nevertheless we pay up to 80 per cent in each of these countries on our profit, and rightfully so.

The CHAIRMAN. Do you mean to say each of these countries in which you manufacture these radiators and these war supplies has an 80 per cent tax.

Mr. HAMILTON. A maximum 80 per cent rate, the same as is proposed in this country. But I made the remark in passing that the exemptions are more generous.

The CHAIRMAN. I did not know that all of those had practically the same.

Mr. HAMILTON. They have now. France raised hers from 60 to 80 last year.

Senator NUGENT. Will you be kind enough to furnish the committee a statement showing the profits derived from the manufacture of munitions, as well as those derived from the manufacture of radiators and boilers?

Mr. HAMILTON. Yes; I will be very happy to do so. I might say that our final net profit last year was materially less than 10 per cent of the actual value of the assets employed in the business. I want that to go in the record.

Senator SMOOT. In this country, as well as foreign countries?

Mr. HAMILTON. In foreign countries. I am not prepared offhand to speak of this country. It is around that figure. I think it was 11.64 in this country.

After paying an 80 per cent excess-profits tax over there, and bringing what is left over here and then paying 80 per cent on that, it leaves 4 cents on the dollar. Of course, I am not oblivious to the fact that we have certain exemptions before we get up to the 80 per cent. But each of those companies, as well as the parent company, assuming the present bill before this Congress becomes effective, will be up to the 80 per cent bracket, and consequently my statement is literally true.

Senator SMOOT. There is not any doubt about it at all.

Mr. HAMILTON. We can not bring dividends in from the foreign subsidiaries unless a compensating advantage is given them through the element of invested capital or prewar profits. That is my point.

Senator SMOOT. In other words, your company can not afford to take all of its gains in the foreign country for the privilege of getting 4 per cent of the gains?

Mr. HAMILTON. Exactly so. The case is so apparent that it scarcely requires elaboration. And the bill as written has absolutely no offsetting or compensating advantage for that investment.

Senator SMOOT. And the only alternative is to not declare the dividends?

Mr. HAMILTON. The only alternative is not to declare the dividends, and it is perfectly apparent that there will be no more dividends.

The CHAIRMAN. What is the law with reference to dividends in these foreign countries? Is there any permission there to retain a part of the dividends and pass it to surplus?

Mr. HAMILTON. I should like to be better advised of the facts through our European manager, who is arriving in Washington

this afternoon, to speak conclusively. But I understand—and this is confirmed by my monthly observation of the balance sheet of our French company—that they permit a 5 per cent reserve to be set aside specifically as a reserve without taxation.

Senator SMOOT. That is 5 per cent on the capital, not 5 per cent on the gain?

Mr. HAMILTON. Five per cent on the capital, I believe it is. But I hesitate to talk on that subject without the investigation.

The CHAIRMAN. Are you going to furnish the committee evidence with regard to that?

Mr. HAMILTON. I should be very happy to. This has all come up so suddenly there has been no opportunity for investigation.

Senator SMOOT. Let me suggest to you that you make a brief, and in that brief answer the questions that have been asked you in this hearing, and file it with the reporter, to be a part of your remarks.

Mr. HAMILTON. I shall be very happy to do that.

The CHAIRMAN. Suppose you take a concrete case, including the operations of one of your subsidiaries in France or England, and work out the amount of taxes you will have to pay, the exemptions, etc., so that we can have the facts with reference to that case before us.

Mr. HAMILTON. Yes. I shall take either our French or our English company.

The CHAIRMAN. Follow up your net income from that source, and what would happen to that if it were brought over here.

Mr. HAMILTON. There is a very interesting and odd situation in the Italian law, whereby they are not allowed to send out of the country dividends greater than 8 per cent on the capital stock.

Senator SMOOT. Capital invested?

Mr. HAMILTON. They have held it as capital stock in our case, and it is very close to the same thing.

Senator SMOOT. Is there another point you desire to speak of?

Mr. HAMILTON. I have another point of an entirely different nature I would like to present.

The other point, perhaps, concerns the American Radiator Co. less than the average company. But it is a point in which we, as a representative firm, with the interests of our own concern and the business world at large before us, feel should be presented to this committee, and although we are self-chosen in presenting it, we trust it will be accepted as on behalf of the business world at large.

It is the case presented by the inflation of inventories, which means, in our business parlance, finished products, raw material, etc., through the inflation of inventories at this time. The most casual inspection will show that raw materials have increased in value since the pre-war period on the average between two and one-half and three times. There is a formula which holds. Take wool, copper, wheat, and pig iron, those four typical raw materials, and it will be found in each case that the present price is approximately two and one-half to three times the prewar price. It is quite apparent with wheat. I believe the price before the war has been said to be 92 cents. The present factor is approximately two and one-half times, and the same runs through. Cotton, I believe, will be bound to be somewhat above that factor.

It simply means that the entire industrial structure of America to-day in its inventories is built upon these inflated values. On these inflated values profits are made, dividends are declared, and taxes are paid. A day of reckoning, we feel, is surely coming.

Senator SMOOT. It is indeed coming.

Mr. HAMILTON. We know not, of course, whether these inflations will come down to the former price, or below, or will strike on equilibrium somewhere between the prewar price and to-day's price. Be that as it may, there will surely be a deflation, and our query is, What is going to happen to American business when the day of deflation comes, if in the meantime there have been no reserves set aside, not only on the books of these concerns, but, perhaps, it should be a real, liquid reserve, to meet this contingency or calamity, as it may prove to be? We feel that our income-tax law practically makes this necessary conservation impossible. In the first place, it is going to take away the profits up to 80 per cent past a certain point. Then it is going to so penalize the concern for retaining even its exempted or remaining profits, if it does not pay those out as dividends, that it is going to be the rare concern which will have the financial ability or the courage to maintain a sufficient reserve in liquid form to meet this day of reckoning.

Senator GORE. Do the British make any provision for that?

Mr. HAMILTON. I am unable to answer that, Senator Gore, except in this way, that the British have worked out their income and excess-profits taxes, as it appears to us—and we say this without criticism, because we have as our interests there as truly as here—in a way which gives recognition to the demands and to the needs of the individual case, and of industry, as a whole, through wise exemptions, through liberal allowances for current depreciation, and even more liberal allowances for war depreciation, and through a multitude of small ways, which I am not prepared at this moment to enumerate, it appears to us, in our conduct of a very large industry in England, that they are making it possible, if not through specific action of law, through the resulting effect, to build up safeguards against the future.

Senator GORE. They vest a large discretion in their officers and boards, do they not?

Mr. HAMILTON. Very large, indeed.

Senator GORE. Making it more flexible in individual cases.

Mr. HAMILTON. But that discretion, Senator Gore, does not lie so much with the individual officer as it lies with the rulings made along class lines.

Senator SMOOT. The exemptions in England and all the other countries are a great deal more than we have ever allowed.

Mr. HAMILTON. Hugely more.

Senator SMOOT. Not only that, they are based upon the most prosperous years that England ever had in her whole history, and ours based upon the business when business was almost at a standstill.

Mr. HAMILTON. Perfectly true.

Senator TOWNSEND. Mr. Hamilton, it seems to me that there is a related question here, which has been brought to my attention several times. Here is a man who was in business, we will say in the wholesale merchandise business. When the war broke out he had a

large stock of goods on hand at prewar prices. My attention has been called to one case in particular, where immediately, when prices raised, he, of course, marked up the price of the goods on the shelf that had been bought in the prewar period. He had an advantage there that the war brought him, which resulted in very large profits, immense in some cases.

Mr. HAMILTON. Yes.

Senator TOWNSEND. Does that offset to any extent this question of high-priced inventories?

Mr. HAMILTON. That, Senator, should offset it very materially, if the people who were the recipients of those, we might say, unearned increments—it is not an unearned increment, as economists know that term, but that expresses it very well; it is not a trading profit, at least, it is a nontrading profit—if they foresaw this thing, and wisely set that aside, and did not declare it out in dividends, or did not foolishly spend it, or did not put it back in any of their plants, and did not turn around, as most of them did, and put that profit back in more goods at the then price, and have continued to compound the operation.

Senator SMOOT. They either had to do that or go to the bank and borrow money to buy the goods.

Mr. HAMILTON. To-day, and beginning last year, I might say, that situation has stopped, of course, the tax laws here taking care of the situation very wholesomely. I am not contending there has not been a certain lack of foresight, of conservatism, and of prudence on the part of very many business men. In our own company I want to say we have built up a very large reserve against the depreciation of our inventories, and we perhaps less than the vast majority of concerns need any protection at this time. But we chance to know that that is not the situation with the average concern, and we have paid taxes, of course, on the revenue we have set aside.

Senator SMOOT. The increases have been more gradual than the decreases after the war will be. When even peace is in sight and the people know it is coming, prices are going to drop immediately.

Mr. HAMILTON. They went up rather gradually and they will come down rather suddenly.

Senator TOWNSEND. That, of course, is speculative, and, I think, altogether probable. But the fact I mention is a fact. As I say, I happen to know of one case where immense profits were made out of goods that were bought under prewar prices. Now, the Senator from Utah says they have to go and borrow money from the banks to buy more goods. They had those profits.

Senator SMOOT. Or used those. Let me call attention to a case that I know of that will perhaps exemplify the remarks that have been made by Mr. Hamilton.

Senator TOWNSEND. I see the force of your argument all right. Mr. Hamilton, and it has appealed to me many times that there was something in it. But I am thinking about the other end of it, too.

Mr. HAMILTON. There is another side to it.

Senator SMOOT. I know of a merchandise house in the West that, before the war carried a stock of \$2,000,000 of cotton goods only, of every description—common goods and fine cotton laces—and they were wholesalers. To-day the invoice price of practically that same stock of goods would be a little over \$6,000,000 instead of \$2,000,000.

Senator JONES. Has that concern that quantity of goods on hand to-day?

Senator SMOOT. They have that quantity of goods, and the invoices will show it. They did not have any more capital stock than the \$2,000,000. They have borrowed and are borrowing over \$3,000,000 to meet the purchase price of goods. They have to either go out of business entirely or else they have to buy goods at the price they can. Not only that, for any class of goods now that they purchase they have to give an order six months ahead. They have obligated themselves now for over \$2,000,000 worth of goods to be delivered within the next six months. For some of the finer goods they have to give an order nine months ahead, and they have to order them and have to take them at the price they are to-day. The query is: Supposing the war would stop now, they are borrowing more money to-day than their capital stock is, and I had the manager of the institution here the other day wanting to know what is going to happen to them if the war were to come to a close immediately. I know what will happen to them.

Senator TOWNSEND. What will happen to them if it goes on four or five years?

Senator SMOOT. This is what has happened and it will happen again: As the goods were sold they have had to buy goods, and perhaps even at an advance of what they sold the goods for. But all the profits they have made—and they have made profits on the increase—

The CHAIRMAN. They have made profits on the turnover, too, have they not?

Senator SMOOT. But under the bill as we have it under contemplation and as it will pass there is not any doubt of that—those profits will be taken away from them. And then if the goods increase they still have to buy or else go out of business.

Senator JONES. I have listened to remarks of that kind, which come with a good deal of assurance, but there are other economists who take an entirely different view of the situation. They estimate that at the present time everybody is saving in every way possible to buy liberty bonds, and that everybody is going without the necessities of life, as far as he can conveniently do so, that stocks are being kept at a minimum, and that after the war, when they do not have to buy liberty bonds, and when business starts over, instead of having this great depression and all that sort of thing there will be increased activity. There is quite a school of such economists. And whoever is going to read the future is the man who is going to make big profits after the war is over. But I think the fellow who would sell the future short at the present time is just as apt to make a mistake as the fellow who would go long.

Mr. HAMILTON. Might I suggest, Senator, that perhaps the complication in the schools of thought, of which I have heard a good deal, arises in the difference of whether you are talking for the far future or the near future. I do not think a man of us who has red blood in his veins, and calls himself an American, is going to sell short on the long future, or even the near future. But three months is sometimes a long time, just long enough for you to go flat broke, as it proved in 1907.

Senator JONES. That was a financial panic, and I do not think there will be another acute financial panic under our present system.

Mr. HAMILTON. That was accompanied by a terrible depletion of inventory values. We met this same thing with our company then.

Senator JONES. But I do not think that anyone can lay down as an absolute fact any statement as to conditions that are going to prevail after the war is over. I want my friend Senator Smoot to understand that I do not take his statements as the law and gospel of business conditions as they will exist after the war is over.

Senator LODGE. I should hate to invest money in a company that took the view you take of it.

Senator JONES. I would hate to sell short on the supposition that Senator Smoot's prophecy is going to obtain.

Mr. HAMILTON. I have been asked whether there will be any constructive suggestion to make in this particular. I recognize that anything that is said is open to criticism, and that there might be a hundred equally good suggestions. But it would not be fair to say what I have said without at least offering one type of constructive suggestion. But I feel that American business should be allowed some designated percentage of the profits to be tax free, provided the same be kept liquid, and, if you choose, invested in liberty bonds, and, if you choose, deposited with the Federal reserve bank of the Treasury of the United States or otherwise for a designated period, to end, of course, at sometime after the close of the war.

I assume the ordinary good concern would be equally protected by being allowed to carry its own reserve. Other concerns might be tempted to say they would do that for the tax-exemption feature, and not do it. But in some way, somehow—if I had my personal way it would be by compulsion in the bill—American business should be compelled to protect itself in this particular. The man who knows would do it any way; the man who does not know ought to have to do it for the common good.

The CHAIRMAN. Suppose they were allowed that reserve free of taxes and would build up a great reserve, and this great catastrophe that you foresee should not come. I do not foresee any such catastrophe. I must confess. I am not a pessimist as to what is going to happen after the war closes. I do not believe that business is coming to a standstill. I do not believe there is going to be any great slump for a number of years after the war closes. Some think there will be and some think there will not be. But suppose, in anticipation of the conditions that you so seriously apprehend, we allow these corporations and individuals engaged in large business to set aside a fund, which you call a reserve fund, as against this slump in your inventories, and that that condition does not materialize. Is that fund to escape taxation solely because you had an apprehension?

Mr. HAMILTON. I should say not necessarily so.

The CHAIRMAN. What would you suggest about that?

Mr. HAMILTON. If it could be made a working matter—and I recognize the difficulties of it—there is no reason whatsoever that if there be a reserve—and again I want to say this is only one chance thought of how this might be done—and that reserve fund were invested, if you please, in Liberty bonds and deposited with the Treasurer of the United States, it could be returned, less the proportion

of the taxes or less such taxes as would have been paid in the event the future shows that this catastrophe or calamity has not happened, as represented in terms of reduced commodity values. In other words, at the time these reserves are made each year, the amount of income tax saved thereby could be distinctly earmarked—I am certain of that—and it may be that a formula could be worked out whereby at the close of this set period—one, two, or three years after the war—that tax would or would not be returned, depending upon the inventories showing, in terms, in the deflation in commodity values to the corporations concerned.

I should like to say for the record that what I have said is not a premonition based on pessimism whatsoever.

The CHAIRMAN. I think it would be exceedingly unfortunate if you should succeed in getting this country to agree with you in the prediction which you have made. I hope that your feeling about this is not that of the general business interests of the country.

Senator ROBINSON. It is far more likely to occur if business generally feels that way about it and anticipates it.

The CHAIRMAN. That is exactly what I mean. Of course, I do not mean to say that you ought not to give expression to your views here about that question, but I do feel that it would be very disastrous for this country at this time if the business sentiment of this country should become crystallized upon the idea that as soon as the war ends we are to have a great slump which will result in a panic.

Mr. HAMILTON. Do you think, Senator, that that is a fair reflection of my presentation? Are you not confusing two things? I have spoken, and spoken only and solely of commodity values, and you are talking in terms of generalities after the war. I absolutely agree with anything you can say in terms of optimism as to this country for the long pull or the short pull after this war. I am talking in terms of commodity values alone. I do not think the business of this country is going to be dragged down to the depths. I quite agree with you. It has been my observation, in newspaper talk and my discussion of this thing with business men, that it is so easy to make a word of warning regarding a specific economic fact distorted into a cry of pessimism along general lines, and I protest against any such construction of what I have said, because I have not meant it.

The CHAIRMAN. I am very glad to hear you say that. But I thought that when you said your inventories would suffer a disastrous slump, you meant that the general business of the country would be undermined, and we might possibly find ourselves suddenly confronted by a panicky condition.

Mr. HAMILTON. I expect nothing of the sort. In our business I expect, since we are directly dependent upon the building industry, that we will have the greatest boom the world ever knew, because to-day the United States as a whole is underhoused. We know that. And building that is not done to-day is not water that has gone over the dam. It is water that is behind the dam, waiting to come over when opportunity offers. No; I am what is called a howling optimist on the prospects of the building business.

Senator ROBINSON. As to commodities that relate to the building business, then, the end of the war will tend to produce an advance rather than a decline?

Mr. HAMILTON. I can not think so, looking back in terms of history. The 1907 depression is the only one I know, and I realize that that was a monetary panic, and that we have some reason to say it will not happen again. Nevertheless, there has been a working up, an inflation, until something gave way; and, by the way, we are against a pressure now which, in terms of foot pounds, I suppose would be infinitely greater than the pressure at that time, and when the bubble burst, in October, 1907, commodity values went down, just as we fear they are going to do after the war, and yet the year 1808 was the most prosperous year our company ever had, based on building conditions.

Senator JONES. Now, you take the factors that enter into the present condition of inflation. What modification will there be, after the war ceases, to bring about a deflation? The factors which have caused the present inflation will obtain after the war is over. There may not be any increased inflation, but the money, the currency, and the credits of the world will, after the war, be just as great as they are now.

Mr. HAMILTON. Of course, Senator, you are talking of things so big that no one of us has a right to venture more than a modest expression. But, in my own opinion, there is nothing that will have happened during the four or five years of this war, or whatever they may be, to change the fundamentals that obtained before the war. Before this war there were a certain number of people on this earth, with a certain amount of a gold supply, and a certain amount of credit, which, in my humble opinion, is primarily based upon the supply of gold in the earth, as long as the gold standard obtains. I see nothing in this war that, when the war is over, is going to justify the belief that commodity values, in terms of gold, are going to be, on the average, between two and a half or three times what they were before the war. And I ask you the question, what is there about the war that is going to cause a continued inflation of between 250 and 300 per cent in commodity values, expressed in terms of gold, when the gold supply is not increasing?

Senator THOMAS. The momentum which has been produced by the war will carry business activities along for a good while, relatively speaking, after the war, and the depression begins two or three years afterwards. I do not give any specific time, but I think that is the economic fact in history.

Senator LODGE. There is no question of that.

Senator THOMAS. I recall that Mr. Garfield, in one of his very illuminating financial discussions some time in 1867, '68, or '69, said that the expenses of every Government emerging from a war will slowly rise for quite a considerable period afterwards, and the business activities caused by the war will also continue for some time afterwards. Then a period of depression and contraction will set in.

Senator SMOOT. But the contraction in commodity prices begins, if you notice, after every war, nearly at the time peace is declared.

Senator THOMAS. No, I think not. I know that wheat and other commodities, as late as the fall of 1866, sold for more than they did when the war ended.

Senator LODGE. Senator, take the great Napoleonic wars, which are the nearest to this as a parallel. After the great Napoleonic wars, and after peace in 1815, there came the greatest period of distress in England ever known.

Senator THOMAS. True; but not immediately.

Senator LODGE. Very nearly immediately. It reached its greatest in 1819, at the time of the passage of the bullion act, and the distress after the war, within a year or two, was something the like of which had never been known in England. After our Civil War, which affected only one country, we went on for four or five years, as you suggested, and then came what I am old enough to remember, and what you are old enough to remember—though we were both very young men then—the panic of 1872, which prostrated the industries of this country for several years, absolutely prostrated them. We are talking as if we shall get back to the position of 1914. Think of the capital that has been destroyed. Think of the purchasing power that has been killed out of existence, all of which we have to remake. There has been a destruction of capital and credit during this war such as the world has never imagined. Who is going to buy? Who is going to make up those billions that have been burned away on the battle field? You have the vast destruction of capital, the purchasing power, which sooner or later will make itself felt.

Senator THOMAS. It is inevitable, but I do not think it is coming immediately after the war.

Senator LODGE. It may not come the first or second year, but it will come. It is as inevitable as the rising of the sun.

Senator SMOOR. If I were going to deal in commodities I would sell them short. I would not buy cotton at 50 or 60 cents or wheat at \$2.50.

Senator TOWNSEND. This occurs to me, Senator Thomas, as a factor that gives me no little uneasiness. A large part of our capital of our business now is devoted to war purposes. That is, we have millions and billions invested in the production of munitions and such things as that. That can not continue after the war, can it?

Senator THOMAS. No.

Senator TOWNSEND. The readjustment of capital from that business to other business is going to be disturbing, in my judgment.

Senator THOMAS. Unquestionably; but it will not be an abrupt condition.

Mr. HAMILTON. I have only this one further remark to make, in the light of all that has been said, and in answer particularly to the question Senator Jones put, that I feel that to-day our commodity values are based upon the inflated credit produced by the war, and in a considerable degree in this country and in a greater degree in foreign countries upon the inflation produced by their bond issues, and, if I may use the term, their fiat money. If we wish to continue our commodity values in this country after the war on the basis of fiat money, it will be easy, for a while at least. But if we are going to stick to the gold standard of value, it is impossible for me to see how we can maintain commodity values at 250 to 300 per cent with the same supply of gold.

Senator JONES. When the war ceases these expanded credits will not be obliterated, will they?

Mr. HAMILTON. They will still be in existence.

Senator JONES. And be a basis for prices then to the same extent they are now, will they not?

Mr. HAMILTON. It looks to me as if you were taking firmly hold of both horns of the dilemma.

Senator JONES. You will not retire your bonds and you will not retire your certificates?

Mr. HAMILTON. Something has to happen. But you have taken firmly hold of both horns of this dilemma, and sooner or later you will have to let go of one of them after this war. I do not know which one you are going to let go. Either commodity values are going down—that is one dilemma. The other dilemma is, you are going to keep firmly hold of the theory and idea of inflation based upon liberty bonds and money not backed up by gold; and if you stick to the second, I do not care to be a prophet as to what is going to happen.

Senator JONES. We expect gradually to retire the bonds. At any rate, that is the hope of all of us.

Mr. HAMILTON. Where are you going to get the money to do it?

Senator JONES. By taxation.

Mr. HAMILTON. That is why we feel we ought to have a little reserve left now.

Senator TOWNSEND. Are you through with that?

Mr. HAMILTON. I am through.

Senator TOWNSEND. I want to speak about the other point you have made, because I have just received a letter, as I suppose every member of the committee has, from residents of Canada, claiming they are subject to double taxation, and I want to know if there is any difference in your situation in regard to your business there from what the situation is in Great Britain.

Mr. HAMILTON. They are absolutely identical. We own every share of the stock in the factory in Canada. I am not unconscious, Senator, of this difficulty which you will encounter when you try to read this into the law, and perhaps it is a duty to state the other side of the case, which is this, so Dr. Adams of the Treasury Department tells me, and I think it is true, that the fundamental of the present law, and of the new law, will be invested capital, and must be based on first cost, and not appreciated value. We have no argument against that. But this law must not be made so broad that it will allow the man, if you please, who has bought a town lot in Montreal at \$100,000, which purchase has increased through appreciation, and not by sale, to \$1,000,000, to use a million dollars as invested capital. You do not allow that over here, and you should not allow it in your investment over there. By the same token, if we buy for investment, and not in the course of business, 100 shares of stock in the Canadian corporation at \$100 a share, and, still holding it on our books at \$100 a share, it rises to \$200 a share, we should not be permitted to put that in as invested capital at \$200 a share in Canada, because we are not allowed to do it here. But when we put our money in a subsidiary company there, engaged in our own business, our contention is that it should have the same consideration, no more and no less, as a like subsidiary company in this country, in which our earnings therefrom, as reflected by dividends, should be given a proper expression through a proportionate use of their invested capital. I do not mean to contend

that we should be allowed to use the value of these foreign company stocks, or their capital plus their surplus value, their book value, as our invested capital, except when and as to the extent that they declare dividends to us. Do I make myself clear?

Senator SMOOT. Perfectly.

Senator TOWNSEND. I understand you.

Mr. HAMILTON. Otherwise, you will be called upon to give us an allowance for invested capital which, if we do not declare dividends, will not result in any corresponding gain to our Government, which would be entirely unfair.

Senator TOWNSEND. You will submit your suggestion in writing?

Mr. HAMILTON. If you choose to have me do so.

Senator SMOOT. Just the answers to the questions you desire to answer.

The CHAIRMAN. Mr. Hamilton, I want to understand you a little better than I do. I understand that your belief is that at the close of the war there will be a readjustment of commodity prices?

Mr. HAMILTON. A readjustment downward. Whether it will be immediate or more gradual I would not undertake to say positively. But my feeling is that it will be rather abrupt.

The CHAIRMAN. But you do not feel that that would necessarily interfere with the general prosperity of the country; the prosperity would simply be based upon a different condition as to commodity prices?

Mr. HAMILTON. I do not feel that the general prosperity of this country will be affected, except to the extent, perhaps, that this affects it, and what that will be I will not undertake to say. It might be that the effect will be only moderate. I fear that the effect will be for more than a moderate effect.

The CHAIRMAN. So far as the demand for the staple products of this country is concerned, while they may be affected by a discontinuance of war activities, there will be other activities that will in a measure take the place of those activities, which will call for a large demand for these things. For instance, there has to be a world-wide rehabilitation to some extent here, but to a very much greater extent in the warring countries of Europe, and for the purpose of reconstruction and rehabilitation there will be a very active demand for many years for many of the staple products of this country.

Senator LODGE. You do not think that the purchasing power is at all affected by the existence of the war?

The CHAIRMAN. I would not say that purchasing power would not be affected, but what I would say would be that there will be still a great demand for our products, a greater demand, probably, than there was before the war.

Senator LODGE. Who has the money to buy?

The CHAIRMAN. I do not think any money has actually been destroyed.

Senator LODGE. No capital has been destroyed?

The CHAIRMAN. No gold has been destroyed, the basis of money. There is as much gold, and more gold, in the country to-day than there was before.

Senator LODGE. When you come back to the gold standard, then you will have the pinch.

The CHAIRMAN. I was not seeking to get into a financial discussion. What I desired to get from the witness was whether he felt that the adjustment of commodity prices, which he predicts, would necessarily interfere to a very serious extent with world prosperity for a number of years, at least, after the conclusion of peace.

Mr. HAMILTON. Directly answering, I think it will seriously interfere with world prosperity for a period, long or short I know not; but at a very critical period, and in a way which will seriously retard the otherwise natural coming of the prosperity which we feel would be based not only upon the release of material things but perhaps idealistically, as I feel it, on the psychological element, which is going to spring up in the heart of every one of us upon the conclusion of peace. I feel that much of this prosperity we are predicting is going to be based on a psychological ground not wholly on a material ground. If I based it on a material ground I would not be the optimist I am.

The CHAIRMAN. It is a fact that a great many well-informed and far-sighted business men in the country feel that when the war closes we will still have, for at least a short period, a continuance of very decided prosperity in business and very great activity?

Mr. HAMILTON. I am not prepared to say whether that is the consensus of opinion or not.

The CHAIRMAN. I am not asking you if that is not the consensus. I want to know if you do not know that is the opinion of well-informed and far-sighted business men?

Mr. HAMILTON. I do; and in this opinion I share.

Senator GORE. I find it considerably divided. I want to ask you if your proposition is general as to the decline of commodity prices, or do you think special conditions affecting some commodities will rescue them from decline?

Mr. HAMILTON. My rather limited observation, Senator Gore, is that if the chief commodities—iron (which means steel), cotton, copper, and wheat—decline through natural and not artificial causes, the natural causes that cause that decline in those commodities will surely eventuate in the decline of other commodities.

Senator GORE. Unless the natural causes are neutralized in some instance. What I had in mind particularly were the commodities not produced in the central allied countries, but were their prime necessities, such as cotton. They do not produce cotton in the central allied countries. They have a famine of cotton; they are naked. Russia, Turkey, Austria, and Germany will be naked so far as cotton clothing is concerned. It seems to me that will create an extraordinary demand for cotton that might except it out of this general rule and general decline; perhaps copper, too.

Mr. HAMILTON. Copper, too. You might also make the same argument for wheat, and to-day pig iron is being produced in the central powers at an accelerated rate never before known.

Senator GORE. It would not come within the exception, then. Whatever they are producing would not come within the exception.

Mr. HAMILTON. No; quite true. Perhaps pig iron would be an exception to the particular thing you have in mind. But you find that commodity values seem to follow one another through causes which we do not understand. But the currents run deep, and all you

have to do to prove that is to take this situation, which, as I have said, barring cotton alone, and that only in recent times, shows there was a factor of two and one-half times which was almost a constant.

I thank you very much indeed for your courtesy.

The CHAIRMAN. We are much obliged to you, Mr. Hamilton. We will now hear from Mr. W. S. Smith.

AUTOMOBILES FOR HIRE.

STATEMENT OF MR. W. S. SMITH.

Mr. SMITH. Mr. Chairman, I do not think I will take very much time. My object in coming here is to increase the revenue for the Government. We are in the sightseeing business in Boston, Philadelphia, New York, and Washington. When the last war tax was paid I had up with Commissioner Robey the subject of taxing sightseeing cars, and he asked me to present a bill to him, which we did, and I will read it. This is the bill before you.

Senator DILLINGHAM. What section?

Mr. SMITH. Paragraph 11 and paragraph 12, page 143. That it puts it up to the companies to pay the tax. Most of the companies operating are irresponsible. They do not keep books, and operate perhaps two or three months in the year, and it would be pretty difficult to collect it from a great many of them. We believe that sightseeing companies should collect a tax from the passengers they carry, the same as the railroads and steamships. If you calculate all the automobile and bus and stage lines, it would bring in a very large revenue. There is the Yellowstone Park stage line and the Fifth Avenue bus line that do a very large business.

As to automobiles, you have here in Washington dozens of men who own one car only and do a sightseeing business. The bill reported out by the Ways and Means Committee puts a tax on the man owning three cars. He must own three cars before he is taxed. In Boston we have two men who own three cars. They will drop down to two; they will lease two cars to their drivers and escape the tax. One automobile should be taxed doing the same business as the three automobiles.

You have two lines running here—motor lines. One runs to Frederick, and the other runs out here about 33 miles to some city I have forgotten the name of. They are operating 14 cars, carrying passengers. They should pay a tax.

Senator THOMAS. What do you think of Mr. Fitzgerald's suggestion yesterday—of placing a direct tax of \$20 a vehicle upon all vehicles used for the carrying of passengers throughout the country—in place of this?

Mr. SMITH. That would not bring in nearly as much revenue, if it is revenue you want.

Senator THOMAS. He said it would bring in eight or ten times as much.

Mr. SMITH. We are doing a business of \$150,000 a year. We would pay in \$15,000—10 per cent.

Senator THOMAS. What I want to get in is something you can not pass on, if I can.

Mr. SMITH. Something you can not what?

Senator THOMAS. You can not pass on.

Mr. SMITH. Pass on to the public?

Senator THOMAS. Yes.

Senator SMOOT. Then we can not get the revenue.

Senator THOMAS. That may be.

Senator LODGE. You mean something direct on cars?

Senator THOMAS. Yes.

Mr. SMITH. You have a bill which taxes the cars of the company—the Ways and Means bill, page 148.

Senator THOMAS. I understand.

Mr. SMITH. Page 148 taxes every automobile.

Senator LODGE. Those are not automobiles run for hire.

Senator THOMAS. His proposal is to put another tax in place of this 5 per cent tax of \$20 per car upon all cars used for hire.

Senator TOWNSEND. How many cars do you have?

Mr. SMITH. We operate about 25 cars.

Senator TOWNSEND. Then you would pay \$500?

Mr. SMITH. We will pay \$500.

Senator TOWNSEND. What will you pay at 5 per cent?

Mr. SMITH. \$7,500. If the tax is 10 per cent, we will pay \$15,000. If this law should pass, it would drive us out of business, provided it is retroactive.

Senator DILLINGHAM. Yours are the large cars, are they not?

Mr. SMITH. No. We operate 11 and 14 passenger, mostly. We have one 18 passenger car in Washington.

Senator DILLINGHAM. They differ radically from the automobiles?

Mr. SMITH. From the automobiles, yes.

Senator DILLINGHAM. Of the auto service?

Mr. SMITH. Yes. This bill of the Ways and Means Committee, if it was retroactive, would legislate us out of business. It would call for the payment of fifteen or twenty thousand dollars a month, and our business, of course, has been in pretty bad shape since the war. We have had a great deal to contend with. Gasoline, tires, and wages are very much higher, and fares have not been increased. We have not increased any fares.

Senator JONES. But you have had an increased patronage, have you not?

Mr. SMITH. No, sir. Our business in the city of Boston for July and August this year shows a falling off of nearly \$10,000 for the two months.

The CHAIRMAN. Are all of your cars over seven passengers?

Mr. SMITH. No; we have some seven-passenger cars. We have none in Washington. We have none in New York. We have some in Boston.

Senator JONES. I referred to your business here in Washington.

Mr. SMITH. Our business in Washington shows a falling off for August of \$1,076.

Senator JONES. I do not mean in dollars, but in the number of passengers carried.

Mr. SMITH. That would be the number of passengers. It is \$1 or \$1.50 per passenger.

Senator DILLINGHAM. Compare it with the same period last year.

Mr. SMITH. \$1,076 in August, and \$1,057 in July, with greatly increased expenses here.

The CHAIRMAN. You are first objecting to the manner in which the tax is levied. You think it ought to be levied upon the public instead of the company?

Mr. SMITH. Yes; I think so; upon the public.

Senator TOWNSEND. Would you not do that any way?

Mr. SMITH. Put it upon the public?

Senator TOWNSEND. Yes. If this tax is put on, would you not increase the fares?

Mr. SMITH. We would have to increase the fares; yes.

Senator TOWNSEND. You would collect it from the public, then, whether the Government says so or not, would you not?

Mr. SMITH. We probably would; yes; but if they make this bill retroactive it would come hard on the companies.

Senator THOMAS. Then you could not do it as to the retroactive part?

Mr. SMITH. No. And I do not think there is a company in the country, including the Fifth Avenue Bus Co., that could possibly stand it. It would go back to the 13th of June. But the steamships carry people, and the railroads carry people, and the people their increased tax.

The CHAIRMAN. Then I understand you to contend that there is no reason why the tax on the incomes of automobiles should not be as high as upon sight-seeing cars?

Mr. SMITH. It should be just as high, certainly.

The CHAIRMAN. One is 10 per cent in the bill and the other is 5, and when it reaches gross income your idea is that it should be the same in both cases?

Mr. SMITH. Yes; because the touring car does a sight-seeing business throughout the country. You take Washington. Every corner has a car for hire. It is taking the stranger about Washington, showing him Washington. Take Jacksonville, Fla. There are 150 touring cars there. We have a trip to St. Augustine, the same as they do. They should be taxed the same as we are taxed.

The CHAIRMAN. I rather agree with you about that. If it was put on the car, it should be much higher on the sight-seeing car, because it carries more people. But if on gross income, I do not see why there should be any difference. There may be a reason for it, but I do not see it now.

Mr. SMITH. Here is another feature, the carrying of freight by automobile. The Goodyear Rubber Co. carry from Akron, Ohio, to Boston many, many trucks. Every automobile carrying freight should pay the same rate as the automobile carrying passengers. That business is increasing by leaps and bounds.

Senator SMOOT. There is one continual line of automobiles from New York to Philadelphia all the time.

Mr. SMITH. And they should pay a tax.

Senator THOMAS. They do, do they not?

Mr. SMITH. I do not think so.

Senator THOMAS. I think under the present law all such companies coming in competition with railroads are required to pay a tax.

Senator SMOOT. Not the automobile.

The CHAIRMAN. It has suggested that a reason for this discrimination as between these classes of vehicles is that the automobile fares of the city are regulated, while the fares charged by the sight-seeing companies are not regulated by municipal ordinance. What have you to say to that?

Mr. SMITH. The only regulation would apply to taxicabs only, I think, not to touring cars.

The CHAIRMAN. I take it that all automobiles that are employed for hire are regulated.

Mr. SMITH. No.

Senator LODGE. Do you not have to have a license?

Mr. SMITH. We have a license to operate, yes; but we are not regulated. You can hire a touring car for \$3 an hour, \$4 an hour, or \$5 an hour, whatever the man may charge, here in Washington.

The CHAIRMAN. I am not quite so sure about that. My understanding has been that as to these cars that are for hire, hold themselves out for hire, there was a regular schedule of prices fixed by the municipality.

Senator LODGE. There is in almost all cities.

Senator THOMAS. Would it not come under the control of the local utilities commission?

Mr. SMITH. I do not think the touring cars do.

The CHAIRMAN. Have you anything else to present?

Mr. SMITH. I have a proposed amendment to the bill, which reads as follows [reading]:

That there shall be levied, assessed, collected, and paid a tax equivalent to ten per centum of the amount paid.

That the tax as imposed shall be paid by the person, corporation, partnership, or association paying for the services or facilities rendered.

I thank you, gentlemen.

DOGS.

The CHAIRMAN. The committee will hear Mr. A. C. Bigelow.

STATEMENT OF MR. A. C. BIGELOW.

Mr. BIGELOW. Mr. Chairman and gentlemen of the committee, I am the president of the Philadelphia Woolen Textile Association, which is an association comprised of the big textile manufacturing interests of the biggest textile center of the United States; also the second wool market of the United States. I am president of the sheep and wool association, which is now engaged in an effort to increase the sheep industry of the United States. I am also on the board of governors of the National Sheep and Wool Bureau of Chicago. I just want to let you know what my credentials are in the matter.

For three years I have been giving my services, supported by these organizations, for the purpose of endeavoring to increase the sheep population of our country. I presume you are aware of the conditions in regard to this industry. I will briefly call to your attention, however, from a bulletin of the United States Chamber of Commerce, the following facts: Our per capita production of sheep in the United States has decreased from 0.80 in 1900 to 0.46 in 1917.

The situation presents itself also in this way: The great reservoir of sheep population for many years has been the great western territory. There is every evidence that in that territory there has been a decrease for the last eight or nine years, and that that decrease is going to continue, on account of various conditions in regard to the encroachments of agriculture and the operation of the grazing homestead act.

In order, therefore, to obtain an increase in the sheep of this country we must bring that industry back to the farming section; we must provide for the multiplication of small units, which is one of the biggest factors in the world in this regard.

The CHAIRMAN. The high prices of the wool and of the mutton have not had the effect of increasing it as against these other agencies that have had a tendency to affect disastrously the industry?

Mr. BIGELOW. At the present time the high prices which are prevailing are a great incentive to the farmers to go into the business. There are a great many obstacles, however, which confront them, and it has been the purpose of our organizations to awaken the farmers to the economic situation, which they were not aware of, to show to them the profit which existed in this industry, and to endeavor to obviate and overcome the obstacles which exist to the increase of the population in the farming sections.

The CHAIRMAN. What I had in mind to bring out was that increase in prices was not helpful so far as the increase in the sheep population was concerned.

Mr. BIGELOW. It was not; no, sir. It was not acting very forcibly.

Senator SMOOT. I want to say this, Senator, that if it had not been for the increase in price the sheep industry of this country, under conditions existing and outlined by the witness, would have been in a worse condition than it is to-day.

The CHAIRMAN. That is probably so, Senator, but the increase in price is more than offset by these other agencies that operate against it. That is what I wanted to bring out.

Mr. BIGELOW. The present condition on the western range is this, that it is populated to its utmost extent to-day. There is no possibility of any increase on the western range. In fact, the continued operation of the causes I mention—the agricultural encroachment and the grazing homestead act—shows that there must be a continuous decline in that section.

One of the great big obstacles to sheep in farming sections has been caused by the depredations of dogs upon the farmers' flocks. In regard to that I wish to call your attention to the fact that the International Harvester Co. sent out over 5,000 questionnaires to all the farmers, and in reply to those letters all but 18 of the 5,000 reported that dogs were the main cause of the scarcity of sheep.

The CHAIRMAN. Do you agree with that statement?

Mr. BIGELOW. Absolutely. I have also sent out my own questionnaires, I have visited all sections of the country, and I have correspondence coming into my office from all sections of the country, which shows conclusively that that is the case.

I also present to you this brief statement from the United States Department of Agriculture, that sheep-killing dogs are not only recognized as the worst enemy of Eastern flock masters at the present

time, but are known to be the principal cause of so marked a decrease in the number of sheep kept on farms.

Here is ocular evidence of what dogs do. I will be pleased to have you examine these pictures. This one shows what occurred in the State of Pennsylvania. It is difficult to get these photographs, but here is an instance that occurred in New England recently.

Senator PENROSE. The Pennsylvania Legislature passed a law last winter putting a tax on dogs which was meant to curtail these depredations.

Mr. BIGELOW. I was instrumental in drafting that bill and putting it through the legislature.

Senator PENROSE. I only wanted to call the committee's attention to the fact that that great State did act on these lines.

Mr. BIGELOW. And it has been recognized that the Pennsylvania law is the best law thus far enacted.

The CHAIRMAN. What is the amount of that tax?

Mr. BIGELOW. The amount of the tax in Pennsylvania is \$1 per head for male dogs and \$2 for females.

Senator SMOOT. We have the same tax in our State.

Senator PENROSE. Is it being enforced?

Mr. BIGELOW. That is the point I want to bring up. During the past three years we have pursued an organized campaign for the enactment of State legislation, and we have met with success. Recently in the State of Massachusetts the proposed bill was turned down at the instance of those people who are particularly and peculiarly dog cranks. But the great trouble with all State legislation, even when enacted, has been in obtaining enforcement, and even as Senator Penrose states now in regard to the enforcement of the Pennsylvania law, located as we are, where we can give the best possible attention to it, and with the Secretary of Agriculture fully authorized to see to the enforcement of the law—and I visited his office the other day—we find that, due to local influences, political and otherwise, which operate through the constables and the agencies therefor, the enforcement of the law is a matter of slow progress. In some cases it has been opposed absolutely. There is now a case which is subject to prosecution where one burgess of one town absolutely ordered the State constabulary out of the town, would not permit him to enforce the law.

Senator THOMAS. Can that be done successfully in Pennsylvania, the State constabulary ordered out of town?

Mr. BIGELOW. It was done in this case.

Senator THOMAS. My impressions have been, from my reading about the State constabulary of Pennsylvania, that it was one of the most effective State police, and one of the most thoroughly capable bodies of the kind in the world.

Senator PENROSE. The State constabulary retreated.

Mr. BIGELOW. I decline to commit myself on that point.

Senator THOMAS. I understood Mr. Bigelow to state that in that instance the order was effective.

Mr. BIGELOW. The burgess made the order, and it is now under prosecution by the attorney general's office. That is all I can say.

The purpose of what I am submitting to your attention to-day is this: The enactment of a provision by which there will be a Federal

tax placed upon the dogs in the United States. The dog is subject, undoubtedly, of taxation, as a luxury at the best, and has been proven by the evidence, which I trust you will accept, that it is not only a luxury, but it is a most destructive agency of the large stock industries of the United States.

Senator THOMAS. Would you not except the shepherd dogs from the operation of this?

Mr. BIGELOW. We except nothing. It has been proven conclusively that a shepherd dog will protect his own flocks and will go off and kill the neighbor's flocks. And it has been proven that little dogs not over a foot or a foot and a half high will kill sheep. There is no dog that will not kill sheep when he gets near them and takes it into his mind to chase them.

Senator PENROSE. Why do the dogs kill so many sheep? Do they eat them or try to devour them?

Mr. BIGELOW. The general process is about like this: Most of the dogs are cur dogs that are not half fed. At nighttime, like all predatory animals, they roam the country seeking something to eat. They destroy birds' nests, they chase rabbits, they invade poultry yards, and if perchance in their roaming they come upon a flock of sheep, the sheep, being so timid, starts to run; the dog immediately, following his instincts, chases the sheep, and from there on goes the destructive result.

Senator TOWNSEND. He does not stop to eat at all.

Mr. BIGELOW. The operation of the measure which I propose, for which I ask your consideration, is this: That to the extent that you lay this Federal tax upon dogs you provide a large amount of revenue, which is undoubtedly needed under present circumstances, upon a luxury, or upon something which is worse than a luxury, a destructive industry.

Senator PENROSE. I am heartily in favor of this tax and recognize the evils. But if it is difficult to enforce it under a State law, would it not be almost impossible to enforce it in the Nation at large, where social and physical and industrial conditions vary so greatly?

Mr. BIGELOW. There is this point distinctly why we propose this Federal measure: Our experience, I think, generally is that when the Federal Government says that a man shall do a thing, it is pretty nearly done. It is not subject to the local influences which I have suggested. And when the Federal tax collector says to any resident of his district that he has to come forward and pay a tax, I know that most of us do it, and that is one of the great virtues of what we propose. By getting the Federal Government to put this on as a method of taxation we shall obtain throughout the entire United States at one time the operation of a law which, by taxing this unessential industry, will tend to discourage the maintenance and increased production of dogs.

Senator TOWNSEND. How many dogs are there in the country?

Mr. BIGELOW. It is estimated at anywhere from two to twenty-five millions.

Senator GERRY. What are you going to do with the cur dogs that do not pay any taxes? If you are going to try to kill them off, will that not require rather large expenditures?

Mr. BIGELOW. The only necessity I see is to impose a tax, and provide for the method of collection, and a penalty for failure to pay the tax.

Senator ROBINSON. You can impose on the owner a penalty for owning a dog on which no tax has been paid.

Mr. BIGELOW. A penalty for nonpayment, the same as for the nonpayment of an income tax.

Senator PENROSE. What does become of the dog if you turn him loose?

Mr. BIGELOW. The dog has a peculiar habit of staying around the habitat of his owner. You can not drive him away. And in that case, in regard to a provision for the law, I would apply the definition employed as to the owner of a dog in the Pennsylvania law:

The word "owner," when applied to the proprietorship of a dog, shall include every person having a right of property in such dog, and every person who keeps or harbors such dog or has it in his care, and every person who permits such dog to remain on or about any premises occupied by him.

Senator THOMAS. What becomes of the dog upon whom the tax is paid? Suppose I have a dog and I pay the tax upon it. What restraint does that tax place upon the dog?

Mr. BIGELOW. A restraint on the dog, so far as the control which we are aiming for, must come through State legislation as a police provision.

Senator THOMAS. Unless a tax is prohibitory, it will not prove entirely effective, will it?

Mr. BIGELOW. A tax of \$2 a head, I feel convinced, from my knowledge of the situation, would act to discourage the maintenance of a great many dogs in this country.

Senator THOMAS. It would not discourage the dog upon whom the tax was paid.

Mr. BIGELOW. It would discourage the owner of the dog from keeping him.

Senator THOMAS. Then where is your revenue?

Senator LODGE. Where there is a known owner who has paid the tax, if that dog proves destructive, or destroys sheep, does not the owner become liable?

Mr. BIGELOW. He becomes liable if there is a State law rendering him liable. We are endeavoring, and will continue to endeavor, to have the State exercise its police power in respect of the matter of control of the dog.

Senator ROBINSON. He would be liable under the common-law rule for depredations by a vicious animal which he maintained. There is no doubt that that.

Senator PENROSE. The result would be that with this tax paid the dogs would be chained up.

Senator LODGE. Yes; a tax-paid dog would be prevented by its owner from doing mischief.

Mr. BIGELOW. Not under the operation of the Federal law.

Senator LODGE. No; but I think that would be the tendency; if a man valued a dog enough to pay a heavy tax on him, he would see that he did not kill the sheep.

Senator JONES. Would you say that that applies in sections of the country where sheep are kept under herd?

Mr. BIGELOW. Yes, sir.

Senator JONES. And where they are not being destroyed by dogs?

Mr. BIGELOW. The real sheep dogs, the shepherd dogs which are of any value, are only maintained on the western ranges. One or two dogs will herd 2,500 sheep. The burden of a tax of \$2 a head will not be too much under those circumstances.

Senator THOMAS. The resistance to this is coming from the sheep raisers who have shepherd dogs.

Mr. BIGELOW. I think Senator Smoot can speak on that point as well as I can.

Senator SMOOT. They are perfectly willing to pay the \$2 tax on their dogs if they can have the other fellows pay a tax on the dogs that kill their sheep.

Senator PENROSE. We have been appropriating a million dollars very recently to destroy the coyotes, and the dog is far more of a menace than all of the coyotes put together.

Mr. BIGELOW. Yes, sir.

Senator PENROSE. Because they are confined to a few prairie sections, whereas the dog is everywhere.

Mr. BIGELOW. Let me impress upon you that it is not only the actual loss or damage which has occurred which is the great factor to be considered, but it is the influence upon people who have seen this damage and know what this menace is, and decline to go into the business because they will not undertake the chance. Let me just give you an incident in my own case showing the application of this. I am interested in the Interstate Livestock Co., which is running 5,000 sheep on the cut-over lands in Michigan. I went into the State of North Carolina and spent three days up in the western section of the State with a view to buying land in western North Carolina. I saw there the finest opportunities for grazing land for cattle and sheep production that I have ever seen in my life—a wonderful country—and land offered to me in tracts of two to ten thousand acres at \$5 to \$10 per acre. I made inquiry there in regard to the conditions as to this one question of dogs. We had a meeting before the board of trade at Asheville, and from the incidents related there, and from my own personal observation the day I drove out to a farm, I changed my mind about buying the land. A man just came back from a lot where dogs had taken his sheep. I learned that North Carolina provides no protection, and there is no provision by which a man who suffers damage can obtain any redress. I decided that the State of North Carolina was not the place for us to buy land to keep sheep on.

Senator DILLINGHAM. How many States have that provision you speak of, where the losers of sheep through the medium of dogs can make claim on the State?

Mr. BIGELOW. I should say probably half a dozen.

Senator DILLINGHAM. What is the effect?

Mr. BIGELOW. It depends on the law. You are drawing me into this, but I am glad to talk to you if you can listen to me. One of the great faults with State laws in regard to this one question of damages has been that they have provided that fines and payments of dog license fees should go into a separate county fund, and that all damages should be paid from that separate county fund. As a matter of record, it has been shown that on account of the local influences which

I say exist the dogs that should have been subject to the license fee have never been licensed and there is no fund in the county to pay it, and therefore a man who suffers damage never receives a dollar, and that we provided for in the Pennsylvania law distinctly, and it has been recognized as one of the main virtues of the law, that all license fees and fines go into the general county funds and from the general county funds the damages are paid. Therefore, the farmer is always assured, because the money is there in the general funds.

Senator LODGE. England and Scotland are densely populated countries. They raise a very large amount of wool. It is a great staple. They keep sheep all over the South Downs of the southern part of England. How do they manage to protect them? It is a densely populated country and it is a population of dog lovers. How do they manage?

Mr. BIGELOW. I am glad you brought that point up. Some of the provisions of the Pennsylvania law were taken directly from the English law, and I had full information from there in regard to the matter. The English law provides very distinctly—and in England that law is enforced—that dogs are not allowed to run at large on the public highways, and at night they must be restricted to the premises of their owner. Ninety per cent of the damage to sheep is done during the nighttime, and the English law in that respect is enforced, and that is the reason why they do not suffer depredations as in this country. One evidence of the enforcement of the English law since that was enacted, about 1894, when they had an outbreak of rabies there, is that there has not been a single case of rabies in the whole of the British Isles, but you can go into North Carolina and Georgia, as I have recently, and those two States are infected from end to end with rabies. I saw in the State department of hygiene in one day 15 cases, and most of them children, being treated by the Pasteur treatment for rabies.

Senator LODGE. England has exterminated rabies.

Mr. BIGELOW. Absolutely, by a strict enforcement of these provisions, which provide that the owner of a dog must keep him on his own premises.

Senator LODGE. In England a dog that is guilty of attacking a sheep is invariably killed. Is there any law about that or is that a mere custom?

Mr. BIGELOW. That I could not say. The owner who allows his dog to run at large is subject to a fine, which operates to keep him where he belongs. That is the great point.

The CHAIRMAN. All you are asking us to do now is to place a Federal tax upon the dog?

Mr. BIGELOW. Yes, sir.

The CHAIRMAN. The effect of that would be, I presume, and that is what you have in view, to induce a great many owners of dogs to kill the dogs?

Mr. BIGELOW. Yes, sir.

The CHAIRMAN. Or otherwise dispose of them in some way that would relieve them of the payment of a tax?

Mr. BIGELOW. Yes.

Senator ROBINSON. The worthless dog, the dog that is not useful for some purposes, or maintained as a pet, would disappear.

Senator PENROSE. This proposition was before us last summer. It is generally treated without sufficient consideration. I think it was one of the most important things before the committee.

Senator SMOOT. I think it is a very important thing. But not only that; there is the dog that the owner compels to go around the country and hunt up its own food, and some of them have a lot of beastly things around, sometimes as many as six, never feed them a pound to live on, and they have to go out and forage and kill to get enough to live on. It will do away with all of that class.

Senator GERRY. How are you going to prove to whom that dog belongs?

Senator SMOOT. If you go into the West and through that country you will find six or seven of just that kind of dogs around one place, many times.

Senator ROBINSON. You could provide that any dog upon which the tax has not been paid should be subject to destruction by any person. Then the owner of sheep can kill the dog.

Senator PENROSE. They capture and destroy dogs in all large cities. Why should they not be captured and destroyed in the country at large?

The CHAIRMAN. If we impose a tax to be assessed against the owner of the dog it would not reach the dog, and it would be within his discretion as to whether he killed the dog or paid the tax and kept the dog.

Mr. BIGELOW. Exactly.

The CHAIRMAN. If he paid the tax and kept the dog, so far as this legislation is concerned, unless it is supplemented by State action, that dog would have the same immunity that the dog now has?

Mr. BIGELOW. Yes. This is simply trying to discourage the increased population of dogs.

The CHAIRMAN. So that unless you followed it up by getting the States to enact legislation—and I concede this action by the Federal Government might lead to quick action by the States—to make the taxes effective I do not think you would accomplish much of a result, except that you would reduce the number of dogs in the country, because a great many people would kill the dog instead of paying the tax.

Senator JONES. Would it be practicable to impose a tax upon unmuzzled dogs, and of such a magnitude that it would be prohibitory? In other words, could we put a tax of \$5 or \$10, or \$15 or \$20 upon any dog that is permitted to leave the premises unmuzzled, or something of that sort?

Senator LODGE. Put a flat tax on all dogs, and then a heavy tax on the unmuzzled dogs.

Senator SMOOT. The unmuzzled dog then would be the dog owned by the sheep owner.

Senator JONES. I mean to go off the premises unmuzzled.

Mr. BIGELOW. I would not recommend that. There is a great objection, a real valid objection, to muzzling dogs, and it is really cruelty. I love a dog as much as anybody in this world, but it is simply a point of controlling something which is a menace to one of the greatest industries in the United States.

Senator JONES. Permitting them to go off the premises unmuzzled would render the owner liable.

Senator GERRY. It would stamp out rabies, too.

Mr. BIGELOW. The control and regulation of the dogs we propose to get through State legislation. I just want to say, Senator Simmons, that in your own State, North Carolina, we have been very busily engaged in obtaining a law. I have a little poster here, which you may not have seen, which is posted all over North Carolina, urging a dog law there which will be proposed at the next legislature.

The CHAIRMAN. I agree with you absolutely that the future of the sheep industry in this country depends upon your getting sheep raised on the farms. That is an industry that has almost disappeared in the country. Before the war every farmer had more or less sheep. Now it is a rare thing that a farmer owns a sheep at all. I agree with you that the dog has been an instrument of destruction, the effect of which has been to induce farmers to abandon sheep raising, and in North Carolina we have not regulated it. But North Carolina does not stand alone in that regard.

Mr. BIGELOW. No, sir.

The CHAIRMAN. I do not know of any States that have regulated the matter of the owning of dogs effectively, and I think very few have. Some States have passed laws, but have not enforced them.

Mr. BIGELOW. I am sorry to say to the honorable Senator from Massachusetts that we regretted very much that the wise people of the legislature turned us down last year. But a recess committee was appointed which is considering the matter, which will be presented to the next legislature.

I want to present to the committee resolutions on this subject which have been adopted by some of the largest organizations in the United States. The Cut-Over Land Conference in New Orleans in 1917, having recognized the live-stock interests as something which are a great factor of production in the South, have passed this resolution.

The American Association of Woolen and Worsted Manufacturers at their annual meeting, the National Association of Hosiery and Underwear Associations at their annual meeting, the United States Food Conservation, live-stock industry division, at their convention here, and the National Association of Retail Clothiers have all passed resolutions, which I will not read, but which urge the enactment of such legislation.

Senator LODGE. Your advocacy of a Federal tax is not with any idea that it is a complete solution of the problem, but it will be a help by discouraging the maintenance of worthless dogs?

Mr. BIGELOW. Absolutely. That is the point. It will simply act as a discouragement to an increased production of dogs.

Senator LODGE. This destruction of sheep does not come from these dogs of high price and great value, because those dogs are carefully contained and kept within control, of course. I mean dogs like setters; valuable dogs of that kind.

Senator PENROSE. They are generally kept within bounds, or somebody would steal them.

Senator LODGE. They are very carefully guarded.

Mr. BIGELOW. Mr. Chairman, may I make one other remark? At the meeting which was held in Raleigh some time ago not only was this fact brought out in regard to the destruction of poultry, especially in North Carolina, but by a demonstration which extended over

three years in one of the counties in Iowa it was proven that 17 per cent of the hog cholera cases in that district were caused by the disease being spread by dogs.

That is a very important factor wherever there are hogs, and one which should not be overlooked. The dog is a great big economic parasite, and we must control him if we are going to have this industry, which is so essential to our country. And it is not only in connection with war conditions but in connection with the development and the utilization of the lands which exist all over these United States to-day which are producing nothing. I have been through New England. I spent one day in July going over a township in New England where the farmers' sons have left the farms and gone to the cities. It is grazing land, and those farms are being sold because they are nonproductive to the owners and nobody can make them productive unless they can bring sheep upon them. That is the only industry that is going to bring that farm proposition of New England back onto a productive basis.

Senator LODGE. That is true of thousands of acres in the western part of Massachusetts. It would be admirable for sheep raising.

Senator JONES. Another matter occurs to me. Is it not a fact that on most farms there is plenty of feed that goes to waste that would support a small bunch of sheep during the summertime and fall?

Mr. BIGELOW. Certainly. Not only that, but in all sections of our country—because I have seen them—there are tracts of land on farms where there is good land, and these tracts have been neglected until they are growing up to brush. They are becoming a wilderness. I examined one on my last trout-fishing trip in Pennsylvania. A man had land of just that kind upon a hillside, which he could run 50 sheep on to advantage, and he would do it, but he said he could not put sheep on there as long as the dogs were running around wild. He had no protection.

(Documents were submitted by Mr. Bigelow and are here printed in full, as follows:)

Resolved by the Cut-Over Land Conference of the South, representing eastern Texas, Arkansas, southern Missouri, Mississippi, Louisiana, Alabama, western Georgia and western Florida, in convention assembled at New Orleans, La., April 11, 12, and 13, 1917, that:

Whereas it is necessary for the National Government to raise a very large amount of revenue to meet the extraordinary expense of war; and

Whereas it is estimated that there are kept in the United States about 25,000,000 dogs, which are not only a luxury and therefore properly subject to taxation, but which are also a cause of much damage to all kinds of live stock: Therefore be it

Resolved, That we urge upon the Congress of the United States to enact a law placing a per capita tax of \$1 on all dogs as a wise financial and economic measure; and

Resolved further, That a copy of these resolutions be transmitted to our Representatives and Senators in the Congress, with the request that they take prompt action to enact a law levying a Federal tax on all dogs.

RESOLUTIONS ADOPTED BY THE AMERICAN ASSOCIATION OF WOOLEN AND WORSTED MANUFACTURERS, AT THEIR ANNUAL MEETING HELD IN NEW YORK CITY ON WEDNESDAY, DECEMBER 5, 1917.

Whereas the enactment by Congress of the law known as the grazing homestead act is operated to force a liquidation of the western-range flocks of sheep in the States covered by the act; and

Whereas the present alarming conditions of the cattle and sheep industry demand that these industries be encouraged and maintained: Be it

Resolved, That we urge that Congress take such action as may be necessary to suspend the operation of the act for the period of three years.

Whereas there is imperative need for a great increase of sheep in the United States to provide both meat and wool; and

Whereas the evidence is conclusive that the depredations caused by dogs upon the farmers' flocks are preventing the maintenance of sheep to a large extent; and

Whereas dogs are mainly a useless luxury and therefore properly subjects for taxation to provide money urgently needed for Government purposes: Be it

Resolved, That we strongly recommend to the Congress that there be levied and collected a revenue tax upon all dogs in the United States of \$2 per head; and therefore be it further

Resolved, That a copy of these resolutions be forwarded to each Member of Congress.

RESOLUTIONS ADOPTED BY THE NATIONAL ASSOCIATION OF HOSIERY AND UNDERWEAR MANUFACTURERS AT THEIR ANNUAL CONVENTION MAY, 1917.

Whereas the sheep industry in the United States has been rapidly declining for a number of years; and

Whereas we deem it an imperative necessity for the welfare of the people of the United States that every effort should be made to increase the number of sheep in our country: Be it

Resolved by the National Association of Hosiery and Underwear Manufacturers in convention assembled, That we cordially indorse the "more sheep and more wool" campaign of the Philadelphia Wool and Textile Association, and that we urge upon all legislative bodies, all trade bodies, and all citizens that they interest themselves in this matter in every way possible to encourage sheep husbandry in the United States.

Whereas the Nation is urgently in need of obtaining revenue; and

Whereas it is an evidence that there are in the United States a vast number of dogs which are essentially a luxury and therefore subject to taxation; and Whereas, moreover, a very large portion of said dogs are not only a luxury but are the cause of great losses to the owners of sheep by their depredations on their flocks: Be it

Resolved by the National Association of Hosiery and Underwear Manufacturers in convention assembled, That we urge upon the Finance Committee of the United States Senate that they include in the revenue bill now being drafted a provision for levying a Federal tax on each and every dog in the United States.

RESOLUTIONS ADOPTED BY THE UNITED STATES FOOD CONSERVATION, LIVE-STOCK INDUSTRY DIVISION, WASHINGTON, SEPTEMBER 5, 6, AND 7, 1917.

Paragraph F:

"The stray and useless dog is the enemy of the sheep. We approve the bill now pending in Congress to impose a Federal tax upon all dogs. We recommend that all State legislatures should enact laws protective of the sheep grower against dog depredations. We suggest that the Bureau of the Census in its plans for the Fourteenth Census provide a schedule for dogs on farms and not on farms."

RESOLUTIONS ADOPTED AT THE ANNUAL CONVENTION OF THE NATIONAL ASSOCIATION OF RETAIL CLOTHIERS, AUGUST 16, 1918, IN THE CITY OF NEW YORK.

Whereas there is urgent need for an increase in the number of sheep in the United States in order to provide the raw material of wool for woollen goods for clothing and to provide meat for food; and

Whereas there is urgent need on the part of the National Government for increased revenues to meet the expenses of the war; and

Whereas careful estimates disclose that there are approximately 20,000,000 dogs in the United States, the maintenance of which should be classed as a

luxury, and therefore a proper subject for taxation; and, moreover, in view of the fact that dogs consume a large amount of food and are recognized as the worst enemy of the sheep industry at the present time, thereby deterring our farming population from an increase of flocks: Be it

Resolved, That, through the proper channels, a copy of these resolutions be forwarded to each Member of the Congress and to each member of the Ways and Means Committee of the Congress.

(Mr. Bigelow subsequently submitted additional information in the form of a memorandum, which is here printed in full, as follows:)

FEDERAL TAX ON OWNERS OF DOGS.

Referring to information and arguments, which I presented to your honorable committee at the hearing on September 14 last, I beg to submit herewith, in conformation, a short brief on this proposition:

The war conditions and general economic conditions have brought a tardy recognition of the great importance of the sheep industry to the United States as an essential branch of live-stock industry—producing meat for food and wool for clothing.

There has been an alarming decrease in the sheep population of the United States since 1900, as shown by the following figures:

Year.	Human population.	Number of sheep.	Sheep per capita.
1900.....	75,994,575	61,503,000	0.80
1917.....	106,000,000	48,483,000	0.46

The decrease of production in the great grazing areas of the Northwest has been due to a decrease in the range areas available for grazing purposes, caused by the encroachment of agriculture and by the enactment of the grazing homestead act. There is evidence that this decrease of production in this section will continue. The decrease in the farming sections, which consist mainly of the area east of the Mississippi River, has been due largely to the depredations of dogs upon the flocks, for which statement I quote the authority of the United States Department of Agriculture, Bulletin No. 935, *The Sheep-Killing Dog*.

"Sheep-killing dogs are not only recognized as the worst enemy of eastern flockmasters at the present time, but are known to be the principal cause of so marked a decrease in the number of sheep kept on farms. The moral effect upon all persons who have seen sheep killed, injured, or frightened by dogs is far more destructive to the industry than the actual damage sustained."

In connection with decreased sheep production in the United States, it should be noted that the world's production before the war had shown a decrease, caused by limitation of available grazing area, and that during the operation of the war, due to military operations, there has been a decrease in the world's sheep population of 54,000,000 head, and this decrease is still continuing.

It would seem that a wise national policy should provide for every possible encouragement of an industry which produces the fundamental necessities of human existence—food and clothing made from wool.

FEDERAL TAX ON OWNERS OF DOGS.

It is a wise national policy to produce on our own lands, which are abundantly available for this purpose, those materials which will make the Nation independent for military requirements in war, and which will make our textile industries independent for the raw materials of manufacture in peace.

On account of the limitation of the western grazing area previously noted, the only source of increase lies in the farming sections east of the Mississippi River. It is in these sections that the depredations of dogs have proven the greatest obstacle to the sheep industry. It has been exceedingly difficult to obtain State legislation to eliminate these depredations, and when legislation

has been secured, the enforcement thereof has been lax and the results unsatisfactory.

Under the present war emergency, therefore, the proposed measure for a Federal tax on dogs would serve two purposes: First, by levying a per capita tax on the owner of a dog for every dog kept, it would provide needed revenue. Second, the imposition of such a tax would undoubtedly eliminate a large number of worthless dogs, and would thereby generally operate efficiently to decrease the present menace which exists to the sheep industry, and also to poultry, hogs, and other live stock.

There are great areas of land in the South adapted to the sheep industry, which are not put to use for sheep to-day, on account of this dog menace. There are thousands of abandoned farms in New England, which do not maintain sheep, for the same cause. There is a wonderful opportunity, moreover, throughout all our farming sections for the maintenance of sheep, to produce meat and wool, and to build up depleted soil fertility, which would result in a greater agricultural production of cereal foods.

The vast burdens of the present war must be met by an increase of national income over national expenditure. Every possible source of increased production should be utilized for that purpose.

It is the urgent appeal of everyone who has a thorough knowledge of the sheep industry, and who is interested in its advancement, that the Finance Committee of the Senate may recognize the gravity of this situation, and may incorporate the proposed Federal tax on dogs in the war-revenue measure now under consideration.

Respectfully submitted.

MORE SHEEP MORE WOOL ASSOCIATION OF THE UNITED STATES,
A. C. BIGELOW, *President*.

AMORTIZATION.

The CHAIRMAN. Mr. Allport, the committee can now hear you.

STATEMENT OF MR. JAMES H. ALLPORT.

MR. ALLPORT. Mr. Chairman, Mr. Edwin B. Chase appears with me to-day, and the question I wish to bring to your attention is the amortization of the costs of material, machinery, and equipment compared at the present time with those of the prewar period and the influence it is having at the present time upon the production of bituminous coal, and also anthracite, in the United States.

The question in particular is for expansion and development, improvements which are necessary in mining, which is a hazardous occupation.

Senator PENROSE. I want to explain to the committee that this proposition has been before the committee before. But I want to say for Mr. Allport that he is one of the greatest experts on this line of inquiry that there is in the country, and I hope the committee will give special consideration to what he has to say and ask him any questions they desire to.

MR. ALLPORT. Being a hazardous industry, expenditures have to be made for improvements and developments in order to maintain production. The cost of material, as you understand, has increased from 100 to 300 per cent, particularly in production machinery, tracks, copper, all electrical equipment, mine supplies, and material which is necessary for not only the increased production of the mines but for the maintenance.

We find, in making out our reports for taxes, that the capital invested in the industry has been capitalized by the Treasury Department for all expenditures, so that it has made it almost impossible for

a producer to increase his production, or to go ahead with additional development, on account of the expenditures being capitalized and taxed.

I have a brief report of which I will read a part to you [reading]:

We find in reports of the probable wording of the new war-revenue bill and in the ruling of the Treasury Department a strong tendency to put costs of certain necessary mine work usually paid out of earnings to capital account and thus increase the taxable earnings.

This, we believe, is resulting in a curtailment of improvements and developments in the coal mines which will inevitably result not only in checking increases in production but in an actual and very serious decrease in the production.

The operators can not and dare not increase their capital by charging to capital account developments and replacements necessary to maintain production, nor can they thus charge the full cost of extensions and new machinery necessary for increased production and to replace man power by machinery at the present abnormal costs, as they well know that under normal conditions they will be unable to earn the interest charges on such inflated capital.

Under these conditions we would respectfully suggest that influence should be exerted to avoid such a catastrophe, and we would urge that the utmost efforts be exerted to have included in the pending war-revenue bill the following principles:

In all coal mines operating expenses to be deducted from gross earnings shall include all expenditures made during the tax year for—

1. All extensions required to maintain output, including the cost of all labor, materials, machinery, and supplies.

2. All machinery installed to replace human labor, including the cost of installation.

3. The cost, above prewar figures, of all improvements and developments made to increase output, including all labor, machinery, material, and supplies required for same. The cost of such improvements at prewar figures to be charged to capital account.

Senator SMOOT. Then you would not get any tax from the coal producers, if that were the case, would you?

Mr. ALLPORT. Yes, sir.

Senator SMOOT. Why should not that apply to other businesses just the same as to coal?

Mr. ALLPORT. That is a question which I will explain when I complete this.

Senator SMOOT. Excuse me.

The CHAIRMAN. Do you mean the increase in the cost of these things you have mentioned should be deducted from the gross earnings?

Mr. ALLPORT. They should be charged to operating expense—operating costs.

The CHAIRMAN. Then they would represent expense and be deducted from gross income for the purpose of ascertaining the net?

Mr. ALLPORT. Yes, sir; with only the difference in the cost of these materials as above the cost in the prewar period.

The CHAIRMAN. And that applies to all machinery installed, all extension of plant, all machinery put in for the purpose of substituting machinery for man power?

Mr. ALLPORT. Yes, sir.

Senator SMOOT. The Bethlehem Steel Co. has done the same thing, and it was necessary that they do it; in fact, the Government virtually required them to do it. Do you think they ought to have all of their buildings and machinery, as enumerated in that, deducted from their gross earnings?

Mr. ALLPORT. The cost above that of prewar period; yes, sir.

The CHAIRMAN. The bill here rather leaves that matter to the Secretary. It reads [reading]:

In the case of buildings, machinery, equipment, or other facilities constructed, erected, installed, or acquired on or after April sixth, nineteen hundred and seventeen, for the production of articles contributing to the prosecution of the present war there may be allowed a reasonable deduction for the amortization of such part of the cost of such facilities as has been borne by the taxpayer.

Do you think that would not accomplish the result?

Mr. ALLPORT. That would probably accomplish what I have to present. But I will add that in section 215, clause (b), "any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate" is an item not deductible. So far as the bill itself is concerned, one clause practically contradicts the other as to the judgment of the Treasury Department in assessing these taxes. I believe this section is all right, but the exceptions taken in the other section on the items deductible would allow the Treasury Department, in the fixing of taxes, to capitalize this excess cost of material and labor that is required at the present time only to maintain production. The operators have been required in all instances to capitalize this extra expenditure limiting their amortization charges, and in many instances where expenditures were made the operator had to borrow money to pay his income tax, having expended it all for increased development. The industry does not take exception to having the Treasury Department capitalize at present cost figures, but they do take exception to the capitalization of this industry at the present figures, which makes that organization to continue these matters of making new improvements for increased development.

Senator PENROSE. I do not want to interrupt you, but you might state, I think, right here what would be the effect upon the production of coal unless this bill is amended?

Mr. ALLPORT. The production of coal would materially increase, from the fact—

Senator PENROSE. I say if it is not amended, what will be the effect?

Mr. ALLPORT. I beg your pardon.

Senator PENROSE. Unless this bill is amended on the lines you have suggested and will elaborate still further, what will be the effect on coal production?

Mr. ALLPORT. There will be a material decrease in the coal production, and I doubt very much if we will produce in 1919 the same tonnage that is being produced in 1918.

Senator PENROSE. How much reduction, roughly speaking, and as a guess, would you say there will be?

Mr. ALLPORT. I would say that in 1919 they could possibly hold their own; that in 1920 there would be at least a 10 per cent reduction. I am stating this from the fact that I have interviewed numbers of operators and operators' committees. The industry from most of the States of the United States have asked the question, What is being done to increase the production of coal in your particular district? I have been repeatedly told that, "We intended to make improvements and expenditures during this year for the increased production, and to open new mines. But owing to the fact that we were

taxed last year on the capital invested for our improvements at the present value instead of the prewar values, we have decided not to make any further improvements this year."

That has been done. From the fact that when a mining operation is opened either by shaft, tunnel, or drift, the coal is near to the opening at the start; the expense gradually increases as the mine is worked away from the bottom of the shaft, tunnel, or drift, as the case may be. Extensions and developments have to be made continuously. There was exceptional development made during the year 1917 and in the beginning of 1918. I now find that that development is lagging very much, and that it is only because of the increased price, or the high prices of rails, overhead, material, locomotives, mine cars, piping, pumps, machinery in general for the handling of coal, and that the operators are simply working their near coal, and not making these extensions and improvements that should be made to increase the output and increase the tonnage of the country. This is not only from a few districts, but it is general.

The CHAIRMAN. Can you tell the committee what has been the increase of the price of coal since the beginning of the war?

Mr. ALLPORT. Yes, sir.

Senator SMOOT. Is this the wholesale price you are now about to give, or the retail price?

Mr. ALLPORT. The price at the mine.

Senator SMOOT. Have you the retail prices as well?

Mr. ALLPORT. I do not have the retail prices. They would be plus the freights and the drayage, as the case may be, from the different districts in which it is produced.

The CHAIRMAN. I hope that is so, but I doubt it very much.

Senator SMOOT. I wish that were true.

Mr. ALLPORT. This is bituminous coal for which I will give you the figures. The average selling price of bituminous coal in the United States for the year 1916 was \$1.55 per ton f. o. b. the cars at the mines.

Senator SMOOT. What was it in 1914?

Mr. ALLPORT. I do not have the 1914 cost, but it was less. The average selling price of coal at the present time for the United States is \$2.162 f. o. b. the cars at the mine.

The CHAIRMAN. That is bituminous?

Mr. ALLPORT. Bituminous; yes, sir.

The CHAIRMAN. Have you the price of anthracite?

Mr. ALLPORT. I do not have the anthracite prices. In 1917 the prices were very highly inflated because they were not controlled.

The CHAIRMAN. In 1917 they were what on bituminous?

Mr. ALLPORT. \$2.162.

Senator SMOOT. I thought that was now.

Mr. ALLPORT. Yes; right now.

Senator SMOOT. That is 1918.

Senator NUGENT. What were they in 1917?

Mr. ALLPORT. We do not have the average prices for 1917, from the fact that the contracts that existed from the latter part of 1916, and the high prices until the contracts expired in 1917, were so irregular all over the country that we have not been able to compile that data and get the exact figures as to what the average cost was.

Senator NUGENT. It was considerably higher than this year?

Mr. ALLPORT. Yes, sir; very much higher than this year.

Senator JONES. Is that for mine-run coal?

Mr. ALLPORT. Yes, sir; the mine-run prices.

The CHAIRMAN. You say you have not the prices of anthracite. About how much does that run above the bituminous coal?

Mr. ALLPORT. The present prices for anthracite coal f. o. b. the mines are \$4.90 for broken, \$4.80 for egg, \$5.05 for stove, \$5.15 for nut, and \$3.75 for pea.

Senator LODGE. Those were the prices agreed on in April, 1917, were they not?

Mr. ALLPORT. Yes, sir; with the additional price that was allowed by the President in the increased price in wages to the miners.

I do not have the prewar prices of anthracite, or any of the anthracite lists, but anthracite coal has advanced less per ton f. o. b. the mines than any other commodity except potatoes since the war.

Senator ROBINSON. How do you arrive at that unless you know the basic figures to start with? How do you know that is true unless you know what anthracite coal was selling for at the beginning of the war?

Mr. ALLPORT. I do not happen to have those figures you ask for.

Senator ROBINSON. You made a calculation based upon those figures?

Mr. ALLPORT. Yes, sir.

Senator ROBINSON. You can easily get those figures?

Mr. ALLPORT. Yes, sir.

Senator ROBINSON. You will supply them to the committee?

Mr. ALLPORT. Yes, sir.

Senator PENROSE. Mr. Allport is a bituminous operator, and came down here to speak for the bituminous people.

Senator ROBINSON. Yes; I understand that.

Senator JONES. What is the price of bituminous coal in the field where you operate?

Mr. ALLPORT. The selling price?

Senator JONES. Yes; at the mines.

Mr. ALLPORT. \$2.95 f. o. b. the cars at the mines.

Senator JONES. How much was that price before the war?

Mr. ALLPORT. That price before the war ranged from \$1.35 to \$1.50 per ton.

The CHAIRMAN. Is that all you desire to say, Mr. Allport?

Senator PENROSE. Have you anything further to say to the committee? You have been interrupted a good deal. Maybe you had better go ahead in your own way for a few minutes.

Mr. ALLPORT. In addition to that I would say that an addition for mining hazards, if actually set aside in cash or invested in liberty bonds of not exceeding 2½ per cent of the value of the coal at the mines, should be allowed.

That is a question which is of vital importance to the industry, and is not allowed by the Treasury Department, from the fact that the accountants of the different departments of the Government said that you should not make a charge into your cost of production for something that has not occurred. Therefore charges that were made into accounts of companies for a hazard such as a mine explosion, a flood, a mine fire, or something of that kind, they would charge from

2½ to 6 and 7 cents a ton on their production, which was carried in a reserve fund for that hazard. That was entirely capitalized by the Treasury Department, on which taxes have to be paid.

The CHAIRMAN. Was it formerly and is it now a general custom among mine owners to set aside a fund of that sort as a reserve against accidents of the character of which you speak?

Mr. ALLPORT. I would say in 50 per cent of the production in the United States that is the custom. The amount that they set aside varies in the different fields—that is, gaseous and nongaseous fields. In gaseous fields it is rather high and in nongaseous fields it is low.

Senator JONES. Is there any limitation on the fund as to amount?

Mr. ALLPORT. Per ton of coal produced.

Senator JONES. Suppose you do not have any accident. Do you keep on piling up the 2½ per cent or any other percentage?

Mr. ALLPORT. Some of those funds have gotten very large in some companies, and yet the majority of the companies in the United States to-day who have had the catastrophes are away behind. The fact of the matter is they have had to capitalize. I know of a number of instances where mine fires are capitalized to-day; floods have been capitalized, catastrophes have been capitalized and are still being paid out from this contingent fund.

The CHAIRMAN. Can you not insure against contingent losses of that sort?

Mr. ALLPORT. No, sir.

The CHAIRMAN. Then this is a sort of an insurance fund?

Mr. ALLPORT. It is an insurance fund; yes, sir; as a contingent fund.

Senator JONES. There is a mine insurance for employees?

Mr. ALLPORT. Employees' liability; yes, sir. For accidents of that kind you can take out insurance, but you can not insure against the property damage, which is really the greater expense of the two.

The CHAIRMAN. Senator Jones asked you about that, but I have not understood your answer to him. Is that a fund of indefinite amount, or do you limit the amount of that fund, and when it reaches that amount do you discontinue then setting aside this amount annually?

Mr. ALLPORT. Yes, sir.

Senator PENROSE. Have you anything further to submit to the committee?

Mr. ALLPORT. I have nothing further.

Senator PENROSE. Have you any brief or figures you want printed?

Mr. ALLPORT. Yes; I would like to submit this.

(The document, submitted by Mr. Allport, is here printed in full, as follows:)

SEPTEMBER 14, 1918.

SENATE FINANCE COMMITTEE,
Washington, D. C.

GENTLEMEN: We find in reports of the probable wording of the new war revenue bill and in the rulings of the Treasury Department a strong tendency to put costs of certain necessary mine work usually paid out of earnings to capital account and thus increase the taxable earnings.

This, we believe, is resulting in a curtailment of improvements and developments in the coal mines which will inevitably result not only in checking increases in production but in an actual and very serious decrease in the present production.

The operators can not and dare not increase their capital by charging to capital account developments and replacements necessary to maintain production, nor can they thus charge the full cost of extensions and new machinery necessary for increased production and to replace man power by machinery at the present abnormal costs, as they will know that under normal conditions they will be unable to earn the interest charges on such inflated capital.

Under these conditions we would respectfully suggest that influence should be exerted to avoid such a catastrophe, and we would urge that the utmost efforts be exerted to have included in the pending war revenue bill the following principles:

In all coal mines operating expenses to be deducted from gross earnings shall include all expenditures made during the tax year for—

1. All extensions required to maintain output, including the cost of all labor, materials, machinery, and supplies.
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3. The cost, above prewar figures, of all improvements and developments made to increase output, including all labor, machinery, material, and supplies required for same. The cost of such improvements at prewar figures to be charged to capital account.
4. An allowance for "mining hazards," if actually set aside in cash or invested in Liberty bonds, of not exceeding 2½ per cent of the value of the coal at the mines.

We believe that if the above can be included in the war revenue bill the result will be to permit and encourage substantial increases of output, which, under the law as now proposed and as interpreted by the Treasury Department, would not and could not be attained, and we believe, unless action of this sort is taken, that instead of the necessary increase an actual and probably serious decrease of production will result.

Further, with such a law, the taxable income of the mines will, we believe, yield a far greater revenue to the Government than will be yielded if development and extension is penalized by putting these charges into capital.

Yours, very truly,

JAS. H. ALLPORT.

PUBLIC UTILITIES.

The CHAIRMAN. Mr. Phillip H. Gadsden is present, and we will now hear him.

STATEMENT OF MR. PHILIP H. GADSDEN, OF WASHINGTON, D. C., CHAIRMAN OF THE NATIONAL COMMITTEE ON PUBLIC UTILITY CONDITIONS.

MR. GADSDEN. Mr. Chairman and gentlemen, I am chairman of a committee known as the national committee on public utility conditions, representing all of the electric railway, gas, and electric-light and power companies in the United States, through their three national associations. I appeared before the committee, you recall, in connection with the War Finance Corporation bill. I also had an opportunity to appear before the Ways and Means Committee on this bill, and I think I could shorten what I have to say by referring to the statements made at that time, which are available, of course, to this committee.

Our purpose in appearing before the committee is to suggest for your serious consideration the wisdom of segregating public utilities into a special class for the purpose of national taxation. We appreciate, of course, that that is not a very congenial suggestion to you, because you are here to raise money. At the same time this is, from our standpoint, as we view it, a great national question, and the problem I want to submit to you is whether the money which

could be raised by applying this normal income tax to public utilities can not be put to wiser and better use by leaving it where it is.

Senator SMOOT. Very few public-utility corporations are making any money.

Mr. GADSDEN. I am talking about the normal income tax, not excess or war profits. Our suggestion is that the public utilities be placed in a special class and their normal income tax be left as it is now, instead of being increased up to 12 or 18 per cent.

The situation of the railways particularly, and in a lesser degree of the gas and electric companies, is that they have not any excess profits to pay on. They are the one industry in this country apparently which is being penalized by the war. Your hearings have been taken up by representatives of the great interests criticizing the percentages of excess profits. We only wish we had profits enough to pay some percentage on. The great industry I am representing, which represents an investment we estimate of about \$10,000,000,000, not stock and bonds, but real money investment, which has a gross receipt of one billion and half, is being destroyed by the war.

The Internal Revenue Department figures show that the total tax in 1916 under the 2 per cent law paid by public utilities was a little over \$5,000,000 on a net of \$250,000,000. Since that time, of course, that amount has been greatly decreased. I estimate that \$250,000,000 net would certainly not exceed now \$125,000,000 net.

The proposition in the House bill is to impose a tax of 12 per cent on such portion of that net as is distributed by way of dividends and 18 per cent on such as is not. That is a part that I wish especially to direct your attention to, because it operates especially against the public utilities. We have come to a point throughout this country when as a class we have passed our dividends. We are husbanding every dollar of resources we have, first, for the reason that we can not borrow any money from a bank. You know the War Finance Corporation will not lend us any, and yet under the losses under which we operate there are daily demands upon us for extensions, betterments, and improvements, which under the law we have to make.

A consumer applies for a new gas connection costing \$5, \$10, or \$15. We have to put it in. An electric consumer wants his house connections made or a new motor put in. The law requires us to do it. In the aggregate that runs into millions. The reports in my office show that, notwithstanding the great economies insisted upon by all of our operating companies throughout the United States, peremptory orders issued to our men in the field not to spend a dollar they do not have to spend, notwithstanding all of that, over fifty millions was spent by us—or I think I would state it more properly if I said, spent for us.

Therefore, what little net we have is all that we have to do this work with. The purpose of this penalty of 6 per cent was to drive the money out into the hands of the stockholders, to in turn come under the surtax, so as to prevent companies from hoarding up their money to be distributed after the war at a lower rate. The situation with us is that we have long since, in a great many cases, stopped paying dividends, in order to husband what little money there is there, to go toward complying with our legal requirements of making

these extensions, betterments, and additional facilities to our service. The war has brought tremendous demands upon railway companies, for instance, for additional cars. In this city they are ordering seventy-odd cars. All through the country it is the same. We can not borrow the money from any bank. Some part of it must come out of our surplus, if we have any. We have very little.

Senator PENROSE. If this is the condition, how can the public-utilities companies, like the Washington passenger railway system, make these enormous raises in wages?

Mr. GADSDEN. Senator, they can not make them.

Senator PENROSE. They have done it.

Mr. GADSDEN. The situation with the railroads to-day is that unless we get Federal relief from the President, which we are very hopeful of getting, and have been hoping day by day and week by week, they are going into the hands of receivers by the dozens within 30 days.

Senator PENROSE. Then they are just raising these wages in order to avoid trouble with their employees, in the hope that they will get Federal aid?

Mr. GADSDEN. Yes; they have to raise them. The Taft-Walsh Board imposed a scale of wages on industry which our office has calculated has involved an additional expenditure of one hundred millions on the railways of the country. When I tell you that under the returns of the Revenue Department for 1916 the entire net earnings of the railways in 1916, as reported to the Revenue Department, were seventy millions—we all admit that increased operating expense of 1917 cuts them down, we will say, to thirty-five million—the Taft Board at one fell swoop added to the operating expenses of the electric railways of this country, when that scale is generally applied, over one hundred millions, and they did not have, according to my estimates, thirty-five millions left.

Senator LODGE. That is Mr. Walsh's board you refer to?

Mr. GADSDEN. The Taft-Walsh Board.

Senator LODGE. Mr. Taft is the chairman?

Mr. GADSDEN. Yes, sir. Of course, the situation was serious in this respect, that we were surrounded by a scale of wages which was taking our men. But, gentlemen, here is a situation where the public utilities, unless relief by the Federal Government is given, are going by the board. We have every reason to believe that some help of some kind is going to be given us, so far as the President can give it. He has shown the deepest concern. We have applied to the War Finance Corporation, and I will tell you what our experience has been. Here is an anomalous case: We go to the War Finance Corporation to borrow some money, under this act passed by Congress, and one of the very first suggestions that is made to us, and in some cases insisted on, is that as a condition of Federal aid, "You waive your dividends. You agree not to pay a dividend until this loan is paid." Then Congress comes in and says, "If you do not pay your dividends, you pay 6 per cent more."

Senator LODGE. We tax you 18 per cent. That is a splendid arrangement.

Mr. GADSDEN. Do you not see that that does not affect industry, but we are the only people who have to go through?

The CHAIRMAN. Did I understand you to say that the War Finance Corporation required as a condition to loaning the money that you should not pay your dividends?

Mr. GADSDEN. I say in many cases they have suggested that, and in several cases required it. I know in many cases I had to go there for assistance. The War Department wanted an extraordinary increase of our power facilities over a long period, and, of course, our company could not possibly do it, and I agree to do it if the War Finance Corporation would make a loan, and one suggestion was that we should waive dividends inasmuch as the collateral I was offering was the stock of the company. I said, "Of course, I can not do that, because the basis of the collateral I am offering you is a dividend-paying stock." But from their standpoint it is a very proper thing, for if a company is in need of funds and applies for Federal aid, they say the stockholders must help by waiving their dividends.

Senator ROBINSON. Did you succeed in making the arrangement in the case you mentioned?

Mr. GADSDEN. In my case I did. That was my collateral, and it destroyed the whole value of the collateral.

Senator LODGE. They ask you to waive the dividends, and then if you do waive the dividends, it is proposed to tax you 18 per cent by way of punishment for waiving them?

Mr. GADSDEN. Yes. That is one feature of it that I think deserves your serious consideration, because public utilities as a class are in that position. We are forced by the exigencies of the situation to pass our dividends.

The CHAIRMAN. You say that the War Finance Corporation required that or suggested that?

Mr. GADSDEN. Yes; that has been suggested.

The CHAIRMAN. The question I wish to ask you is, Do the banks of the country, when you go to secure money through them, make any such suggestion?

Mr. GADSDEN. They make exactly the same suggestion, and from a banker's standpoint it is a perfectly proper provision.

The CHAIRMAN. I am not saying it is not. Is that a general custom among banks?

Mr. GADSDEN. It is under present conditions.

The CHAIRMAN. Does that apply only to the utility corporations because they are in trouble?

Mr. GADSDEN. Because we are in trouble, and we can not pass it on to the consumer.

The CHAIRMAN. That does not apply to others seeking loans?

Mr. GADSDEN. No, sir.

Senator JONES. You say you can not pass it on to the consumer. Is it not just as inevitable as it can be that something must be done to pass it on to the consumer?

Mr. GADSDEN. Unquestionably. But we are going broke in the meantime. One of the things I am asking you to do to pass it on is something within your province. I am going to every department of the Government and saying, "I want you to help so far as you can." This committee can help the public utilities by not increasing our tax burden. We are segregated into a special class for everything except taxation. We are put into a special class for the purpose of fixing

our revenue, we are put in a special class for the purpose of controlling our service, and why not put us in a special class for the purpose of taxation, and say, "Their burdens shall not be further increased"?

Senator JONES. Does what you say apply to all of these public utilities?

Mr. GADSDEN. Yes, sir.

Senator JONES. Are there not some exceptions?

Mr. GADSDEN. Of course, there are exceptional companies; unquestionably.

Senator JONES. Instead of having the plan which you suggest apply in blanket form to all of them, why not vest some authority somewhere to deal with the company which really needs assistance?

Mr. GADSDEN. That accomplishes my purpose. There are some electric railways still which are making money. But I could count them on my two hands.

The CHAIRMAN. I understood you as not insisting that your corporations should be relieved from this additional 6 per cent that the House bill applies upon the undistributed dividends or income of a corporation, but you are insisting that your tax shall not be more than 6 per cent as against 12 per cent normal tax?

Mr. GADSDEN. I am suggesting that we be left as we were last year. You only collect \$5,000,000 out of them under a 2 per cent tax. The amount to the United States Treasury is a bagatelle, but it is all we have. Devoted to public purposes in our hands it will accomplish more than in the Treasury of the United States. It will not amount to more than fifteen or twenty millions in the Treasury of the United States, if that much. But ten or twenty millions to this industry now will help it to go through the war. That is the point. It is on the verge of destruction. And the question of statesmanship and wisdom is whether that money, devoted by us to the public use at this time, is not worth more to the public than turned over to the United States Treasury.

Senator THOMAS. Do the officers of these companies enjoy the same salaries that they did before they got into this fix?

Mr. GADSDEN. I rather think so. I do not know any of them that got any very heavy ones.

Senator THOMAS. What are the salaries?

Mr. GADSDEN. I think in the operating field \$5,000 is a good big salary for the president.

Senator THOMAS. In the New York companies the salary must be very much higher than that.

Mr. GADSDEN. I expect so. But do not judge this industry by the high spots. I am speaking for the little fellows. I am speaking for the men all over the United States.

Senator THOMAS. We have this same appeal, however, from the high spots. I had it personally from two gentlemen from New York only last week complaining very bitterly.

Mr. GADSDEN. They are all suffering.

Senator THOMAS. And I asked what the salaries were, but I could not get any answer.

Mr. GADSDEN. To give you a picture, I have here a tabulation of 293 electric railways, showing their returns for six months. There are four or five hundred in my office, but I just tabulated up to date

the six months as compared with the six months of last year. It shows a decrease in their income during the six months of 74.4 per cent.

Senator DILLINGHAM. That has come from the increased cost of operation?

Mr. GADSDEN. Yes, sir. For instance, the total operating expense of these companies was 11 per cent. Their tax increase was 10 per cent. Yet their gross income had increased $3\frac{1}{2}$ per cent. Notwithstanding an increase in their gross their net income for 1917 was \$11,900,000, and for 1918 it is \$3,000,000. On the 1st of January it will almost disappear, because we have not yet charged up any Taft labor decisions. That is a hundred million going into the situation.

Senator JONES. That net income charge is a most uncertain designation of what may go in it. Your question of expenses and charges and depletion, and all that sort of things, is a matter of judgment for each company, and I suppose your figures there have been made up from the general statements furnished you by the companies?

Mr. GADSDEN. Each individual company sends a report.

Senator JONES. And each company preparing its books in its own way and making its allowances for expenses, depletion, and all that sort of thing?

Mr. GADSDEN. You are mistaken about that. In all States where there are public-utilities commissions there are standard systems of accounts.

Senator JONES. That may be. I do not know about that.

Mr. GADSDEN. All of the large States have them, and the great majority of the trackage is in those commission States. I am not going to detain the committee. It is a question, I respectfully submit to you, that demands wise action on the part of this committee to show some sympathy with this industry.

Senator LODGE. The plain English of it is that if something is not done within the next 30 days the great bulk of the street railways will be in the hands of receivers?

Mr. GADSDEN. Yes, sir. I attended a special meeting called in New York, and it was with some difficulty that some of those men were persuaded to hold on.

This will help psychologically if I can say that Congress has helped me so far as it could. I can go to the executive officers and say, "The political end of this Government is doing all it can." I have to get assistance from wherever I can get it.

Senator PENROSE. How can the Federal Government help you in the executive department?

Mr. GADSDEN. The President can do a great deal.

Senator PENROSE. I know he can do almost everything, but not entirely everything. He is not omnipotent yet. Through what authority of law or in what way can he help the utility companies?

Mr. GADSDEN. I would be very glad if you had time to hear a brief I filed with the Taft Labor Board. I think legally, under the existing statutes and under the state of war, there are two propositions, which I submitted to the board and in which they agreed. The first was that Congress has now the right to fix the rates of public utilities. Second, that under existing legislation that right, so far as street railways are concerned, has been conferred on the President. Mr. Taft and Mr. Walsh both concurred in that.

Senator THOMAS. Do you think the Congress could fix the rate charged by the Denver Tramway Co. in my city?

Mr. GADSDEN. I have not any doubt about it.

Senator THOMAS. I have.

Mr. GADSDEN. I would like to send you a copy of my brief. If Congress can fix the rates of coal in a mine, why can it not fix the rate of the electricity that mines that coal?

Senator PENROSE. Is this brief a voluminous document?

Mr. GADSDEN. No, sir; it is short.

Senator PENROSE. I would like to have it put in the printed testimony.

Mr. GADSDEN. I would be glad to furnish it. It is a novel proposition.

The CHAIRMAN. When you were before us before, you stated, and stated very clearly, that your troubles grew very largely out of the fact that you had been unable to get your rates increased, that they were regulated by the local authorities, and you had not been able to get them to act. The President, I think, wrote a letter in which he urged upon these different authorities the importance and necessity of allowing you to increase your rates.

Mr. GADSDEN. Yes, sir.

The CHAIRMAN. Has there been any response to that?

Mr. GADSDEN. There has been a very substantial response, so far as gas and electric companies are concerned. There has been very little response so far as railways are concerned; almost none.

The CHAIRMAN. And unless you could get your rates increased, nothing can relieve you of your present trouble?

Mr. GADSDEN. Nothing. Unless these rates go up the industry is gone.

(Documents were submitted by Mr. Gadsden, and are here printed in full, as follows:)

AMERICAN ELECTRIC RAILWAY ASSOCIATION WAR BOARD,
Washington, D. C., August 23, 1918.

*Income account of 293 electric railways for the 6 months ended June 30, 1918,
compared with the 6 months ended June 30, 1917.*

	6 months ended June 30.		Increase or decrease 1918 over 1917.	
	1918	1917	Amount.	Per cent.
Total operating revenues.....	\$173,077,841	\$167,211,445	\$5,866,396	3.5
Total operating expenses.....	123,037,864	110,752,026	12,285,838	11.1
Net operating revenue.....	50,039,977	56,459,419	¹ 6,419,442	¹ 11.4
Net revenue from auxiliary operations.....	5,723,679	5,601,684	121,995	2.3
Taxes.....	12,911,593	11,675,740	1,235,853	10.6
Nonoperating income.....	2,365,383	2,040,143	325,240	15.9
Gross income.....	45,217,446	52,425,506	¹ 7,208,060	¹ 13.8
Deductions from gross income.....	42,150,028	40,431,159	1,718,869	4.3
Net income.....	3,067,418	11,994,347	¹ 8,926,929	¹ 74.4

¹ Decrease.

This form is sent to you in duplicate so that one copy may be retained for your files.

ARGUMENT OF P. H. GADSDEN, ESQ., AND BRIEF OF THE WAR BOARD OF THE AMERICAN ELECTRIC RAILWAY ASSOCIATION IN THE MATTER OF THE POWER OF THE PRESIDENT TO FIX RATES OF FARE FOR ELECTRIC RAILWAYS.

Mr. Chairman and Members of the National War Labor Board:

Before reading this brief it will be helpful to the members of the board if I give them a picture of the financial situation and the problems which have been brought upon the electric railway industry by the war.

The public-utility industry as a whole, unlike any other industry in the country, found itself at the outbreak of the war in a situation in which it could do nothing to improve its financial condition. For instance, under franchise regulations and orders of public-service commissions the rate of fare on the electric railways had been fixed years ago, based presumably upon conditions existing at that time. During the many years that electric railways have been operating, their unit fare of 5 cents has had to remain the same, whereas for the last 15 or 20 years their operating expenses have been increasing both for labor and materials. At the outset of the war this recurring and cumulative increase in the cost of labor and materials had made such inroads into the net revenue of the electric railways that very few of them showed any substantial return upon a fair valuation of their property.

Now the war breaks out, and the cost of everything entering in to the operation of those properties, as far as material is concerned, has gone up anywhere from 25 per cent to 300 per cent. The cars that we are purchasing to-day are costing just 100 per cent more than they cost before the war. Every item that goes into the operation of those properties has gone up on a scale with which you are familiar in your own experience.

In addition to that, the same economic principles have applied to the conditions of our laboring men. Their cost of living has increased just as the cost of living of operatives in other industries and other lines of activity has increased. Naturally they have felt constrained to make demands upon the electric railway industry of the country for increases in their wage scale. Already in the 14 or 15 months since the declaration of war a very large number of companies—and I was going to say practically every company—have been called upon to grant increases in wages to their car men. I have in mind a number of companies that have granted three increases in the last year to meet these recurring and extraordinary increases in the cost of living.

In addition to that problem the electric railways in this year 1918 are faced with the necessity of financing maturing obligations, such as bonds issued, say, 20 years ago, maturing in the year 1918, aggregating in the neighborhood of \$125,000,000, and they find at the same time that the financial needs of the Government to carry on this war have practically monopolized all the avenues of finance, so that there is no investment market for public utilities securities. And yet we are faced with the necessity of securing from somebody, somewhere, \$125,000,000 to take care of obligations issued in good faith 15, 20, and 30 years ago.

Some of us during the latter part of 1917 and the early part of 1918, seeing no opportunity of getting Federal assistance in the way of financing, have to go into the open market and buy money. One of the largest aggregations of public utilities in this country, a company operating in 22 States of the Union, was called upon in the early part of January to finance something like eight or ten millions of dollars and was required and forced to pay 13½ per cent for it. Of course, it is needless for us to point out to this board that that means death; that it is simply deferring the inquest until after the war; that no rate which any municipality or any public-service commission will put into effect will be sufficient to take care of a cost of money at 13 or 14 per cent.

Furthermore, there is no national industry of which so much is expected and upon which such great demands have been made in the prosecution of the war. Every industry or factor or navy yard or cantonment or airplane plant or shipyard requires for its successful and efficient operation increased service from some electric railway. When you attempt to visualize the demands that have been made upon the electric-railway industry of the country in handling the hundreds of thousands of operatives at the various munitions plants and shipyards, especially when those plants, as is the fact in a great many cases, have

been constructed at points remote from the centers of the electric-railway systems, requiring new lines to be built, additional circuits for the transmission of the current to be constructed, and extraordinary increases in the power-plant capacity to be provided to handle the business, you get some faint idea of the burdens that are being carried by the electric-railway industry in helping to win the war.

Up to date, under the extraordinary conditions which I have pointed out, under the adverse conditions of a fixed revenue and an increasing operating ratio, in some way and somehow the electric railway industry has performed its duty and has measured up to the standard of patriotic service which the country has called upon it to perform.

We are faced, in addition to the expenditures which have already been made, with increasing demands on the part of the Government, which we estimate will require at our hands at least \$100,000,000 of new capital this year. Where that money is to come from is still a problem. Wherever it comes from, we shall have to pay the interest on it, and to pay it we must earn it; or, to state the proposition conversely, to borrow it we must first show that we have earned it. And, gentlemen, I want to say to you that that is one of the serious problems confronting us in connection with financing through the War Finance Corporation. The directors of that corporation, protecting the interests of the Government, have properly taken the position that unless an electric railway can show sufficient net earnings over and above its operating expenses and fixed charges to create an equity, they are not justified in rendering financial assistance; and yet we must get it for the purposes of the Government. We do not want to make these extensions; we are not seeking, in a time like this, when everybody else is curtailing operating expenses and living expenses, to increase them, but we have got to if this war is to go on.

Now comes the next problem that we face to-day. These gentlemen, referring to representatives of Electric Railway Employees, are here, after all the efforts that have been made during the last 12 months on the part of the companies throughout the country to increase as far as their financial situation justified the wages of their employees, and those employees still finding themselves in a position where their wages are not sufficient under existing conditions, to demand an increase in wages, requiring still further substantial expenditures on our part.

Under these conditions we say again that the situation which confronts us has been brought upon us by the war, that the demands which are made upon us for these extraordinary increases in our facilities are made upon us by the National Government, and that unless we can get relief from the same source we can go no farther.

Now, gentlemen, that is the situation. I submitted to the section a statement of operating conditions, which is on file, and I will not detain the board by going over those figures in detail, but I should like to call the attention of the other members of the board to this situation, that the War Board of the American Electric Railway Association, which was organized to meet just such a condition as this, and whose declared purpose is to coordinate the electric railway industry of the country so as to facilitate the Government's prosecution of the war, sent out a questionnaire to ascertain the operating conditions of the electric railways for the first three months of 1918 as compared with the first three months of 1917. Those figures, which are on file in your office, show that the net income of the electric railways of the country for the first three months of 1908 as compared with the first three months of 1917 decreased 76 per cent, whereas up to the 1st of January they had decreased something like sixty-odd per cent, indicating a progressive increase in the cost of operations and a progressive decrease in the net income.

They further show that, whereas the operating ratio of those properties in 1915 was a little over 60 per cent, for the first three months of 1918 it was approximately 70 per cent.

Now, gentlemen, it is needless for me to dwell upon what that means to you. It means that this industry is heading for the rocks. It means that in six months' time, if conditions are not improved, if revenues are not increased, that ratio will be 100 per cent. Therefore, we have urged upon this board, and in this position the operatives, as represented by the officials of the amalgamated association, have concurred, that the relief which is essential to this great national industry is a proper increase of its fares. We have shown that that relief can not be obtained in proper time through the ordinary channels, for notwithstanding the conditions which the industry has been

going through for 12 months, it is a matter of common knowledge that the percentage of increases allowed in street car fares throughout the country has been pitifully small. That means, and the conclusion is irresistible, that the machinery set up during times of peace for the adjustment and fixing of street car fares is not adapted to meet the extraordinary conditions of war. It was primarily designed to adjust rates downward, not upward. It was properly designed to consume time, so that adjustments should receive the careful attention of all concerned. But now, gentlemen, we are facing a situation which does not permit of delay. The financial situation which I have presented to you, unless relieved within a very short time, will bring about the bankruptcy of this industry.

Now, then, what is the remedy? We submit that the remedy, the only remedy, the only effective remedy, is action by the President, and to sustain that position we have prepared a brief setting out the legal grounds upon which we base the contention that in times of war and national emergency the power is vested in the President of the United States to regulate the rates of fare of the electric railways of the country.

[Brief submitted by the war board of the American Electric Railway Association to Hon. William Howard Taft and Mr. Frank P. Walsh, National War Labor Board, in the matter of the power of the President to fix rates of fare on electric railways.]

NATIONAL WAR LABOR BOARD,

June 25, 1918.

In the matter of the application of electric railway companies that the rates of fare of said companies be adjusted to meet the necessary increases of wages and other operating expenses brought upon them by reason of the war:

At a hearing held this day before the National War Labor Board in the city of Washington to discuss the relation between the financial condition of the companies and the amount of wages to be paid to employees, the representatives of the several electric railway companies present submitted the following:

That the situation of the electric railways of this country is a very critical one, due, among other things, to the fact that they are called upon during the year 1918 to finance approximately \$125,000,000 of maturing obligations at a time when the financial resources of the country have been practically monopolized by the National Government; that in order to provide the additional facilities made necessary by the demands of the war program, they are required to provide new capital to the extent of \$100,000,000. At the same time their operating expenses, due to the extraordinary increase in the costs of labor and material, have already increased to a point when the net income of the companies, as shown by statements filed with the board, has greatly decreased, and is approaching the vanishing point.

It was generally recognized in the discussion that the electric railways of the country were essential to the prosecution of the war, and had an intimate and essential relation to the whole war program.

Applications are now pending before the National War Labor Board by employees of a large number of electric railways for further substantial increases in their wage scales. The representatives of the companies have seriously urged upon the board that the situation confronting the electric railways of this country can only be satisfactorily met by a proper increase in their rates of fare.

The National War Labor Board, as a result of this discussion, has requested the representatives of the electric railway companies and the employees of such companies to submit to said board a plan whereby the largely increased costs of labor and material brought upon said companies by the war may be accompanied by an increase in the rates of fare to be charged on said electric railways, so as to give said companies the necessary added revenue to meet this war emergency.

We respectfully submit to the National War Labor Board that the present emergency can only be met by direct action on the part of the Federal Government, and we believe if the National War Labor Board will approve and recommend the following plan that the necessary relief can be promptly secured:

I. THE CONGRESS HAS THE POWER IN TIMES OF WAR AND NATIONAL EMERGENCY TO REGULATE THE RATES OF ELECTRIC RAILWAYS.

(a) The concentration of the entire activities of the Nation upon the prosecution of the war has brought about a situation whereby practically all of the staple products and the manufactured articles of the country have become

necessary to the prosecution of the war, and the activities of practically all of the great industries of the country have been diverted to that end. The fact that the operations of any industry under the exigencies of war, have become necessary and essential to the Nation's welfare immediately impresses upon that industry a national character and justifies the Federal Government in exercising the Federal power to regulate and control. To state it differently, the power of the Federal Government in a given case over an industry in time of war rests not upon the fact that such industry may or may not be engaged in interstate commerce but upon the more comprehensive basis that such industry, under the demands of war, has become necessary to the Nation's welfare. When such a situation has been created the power of the Federal Government, certainly during the period of the war and for a reasonable time thereafter, is paramount to that of the State.

In pursuance of these principles, we have seen the Government progressively fix the price of wheat, milk, sugar, etc., through the Food Administration; of anthracite and bituminous coal and of coke, through the Fuel Administration; of pig iron, aluminum, steel, cement, lumber, hides and leather, and a large number of other basic articles, through the price-fixing committee of the War Industries Board. Within the last few days a Textile Administrator has been appointed, with large powers over the entire textile industry of the country. Prior to the war the Federal Government did not possess the power to regulate the prices of these articles. How has it been derived? From the increasing necessities of the situation. As each article in turn becomes more and more necessary to the Nation's welfare and more and more intimately connected with the prosecution of the war and the needs of the war program, it comes within the sphere of the Federal control and becomes impressed with such a national character as to justify the National Government in regulating and controlling it.

We are seeking to call your attention to the fact that the power exists in Congress to fix the rates of electric railways. We have seen this power exercised in recent months in the case of the steam railroads. A large increase in the rates of fare has recently been ordered, applicable both to interstate and intrastate rates. This power in the Congress to fix intrastate rates did not spring from the fact that the Government took possession of the railroads, but existed because of the paramount power and duty to carry on the war. Rate making was in that case as it is in this a necessary war measure, and the power to so fix rates exists independent of any other power to take over or operate such properties.

Within the last four months, the fact that public utilities—electric railway, gas and electric light and power—are directly contributory to the conduct of the war and are essential to the Nation's welfare, has been recognized officially by practically every department of the Government—executive and legislative.

In answer to a letter of the Secretary of the Treasury, on the 19th of February the President stated:

"It is essential that these utilities should be maintained at their maximum efficiency and that everything reasonably possible should be done with that end in view."

In his letter to the President, under date of February 15, the Secretary of the Treasury said:

"Our public service utilities are closely connected with and are an essential part of our preparations for and successful prosecution of the war, * * *"

Some time prior to the correspondence between the President and the Secretary of the Treasury the Comptroller of the Currency had declared:

"The continued and increasing efficiency of these corporations is important for the successful conduct of the war. This efficiency is not possible with present conditions. * * * The breaking down of these corporations would be a national calamity."

The act of Congress entitled "An act to punish the willful injury or destruction of war material, or of war premises or utilities used in connection with war material, and for other purposes," commonly known as "the sabotage act," approved April 20, 1918, expressly includes electric railway, gas, and electric light and power plants. "War utilities" are defined in the act as follows:

"The words 'war utilities,' as used herein, shall include all railroads, railways, electric lines, roads of whatever description, railroad and railway fixtures, canal, lock, dam, wharf, pier, dock, bridge, building, structure, engine, machine, mechanical contrivance, car, vehicle, boat, or aircraft, or any other means of transportation whatsoever, whereon or whereby such war material or

any troops of the United States, or of any associate nation, are being or may be transported either within the limits of the United States or upon the high seas; and all dams, reservoirs, aqueducts, water and gas mains and pipes, structures and buildings whereby or in connection with which water or gas is being furnished, or may be furnished, to any war premises or to the military or naval forces of the United States, or any associate nation; and all electric light and power, steam or pneumatic power, telephone, and telegraph plants, poles, wires, and fixtures, and wireless stations, and the buildings connected with the maintenance and operation thereof used to supply water, light, heat, power, or facilities of communication to any war premises or to the military or naval forces of the United States or any associate nation."

(b) This power was recognized and exercised during the Civil War in "An act to provide internal revenue to support the Government, to pay interest on the public debt, and for other purposes," approved June 30, 1864 (13th U. S. Stat. L., p. 223), as follows:

"And be it further enacted, that every person, firm, company, or corporation, owning or possessing or having the care or management of any railroad, canal, steamboat, ship, barge, canal boat, or other vessel, or any stagecoach or other vehicle engaged or employed in the business of transporting passengers or property for hire, or in transporting the mails of the United States, or any canal the water of which is used for mining purposes, shall be subject to and pay a duty of 2½ per cent upon the gross receipts of such railroad, canal, steamboat, ship, barge, canal boat, or other vessel, or such stagecoach or other vehicle: *Provided*, That the duty hereby imposed shall not be charged upon receipts for the transportation of persons or property or mails between the United States and any foreign port; and any person or persons, firms, companies, or corporations owning, possessing, or having the care or management of any toll road, ferry, or bridge authorized by law to receive toll for the transit of passengers, beasts, carriages, teams, and freight of any description over such toll road, ferry, or bridge shall be subject to and pay a duty of 3 per cent on the gross amount of all their receipts of every description. But when the gross receipts of any such bridge or toll road shall not exceed the amount necessarily expended to keep such bridge or road in repair no tax shall be imposed on such receipts: *Provided*, That all such persons, companies, and corporations shall have the right to add the duty or tax imposed hereby to their rates of fare whenever their liability thereto may commence, any limitations which may exist by law or by agreement with any persons or company which may have paid or be liable to pay such fare to the contrary notwithstanding."

II. If the President be advised that the Congress has not as yet passed the necessary legislation and conferred upon him authority to regulate the rates of fare of electric railways, we respectfully urge this board to request the President to seek from the Congress such additional legislation as to give him the power referred to. But we contend that—

III. THE CONGRESS ALREADY HAS CONFERRED UPON THE PRESIDENT THE POWER TO REGULATE THE RATES OF ELECTRIC RAILWAYS.

(a) Joint resolution of Congress, dated April 6, 1917 (Stats., 1917, p. 1), declaring a state of war to exist between the United States and the Imperial German Government, which directs the President to employ the entire naval and military forces of the United States and the resources of the Government to carry on the war.

(b) Joint resolution of Congress, dated December 7, 1917, declaring a state of war to exist between the United States and the Royal Austro-Hungarian Government, and directing the President to employ the entire naval and military forces of the United States and the resources of the Government to carry on the war.

(c) An act making appropriations for the support of the Army for the year ending June 30, 1917, and for other purposes, approved August 29, 1916 (Compiled Stats., p. 3778), which act empowers the President, through the Secretary of War, to take possession and assume control of any system or systems of transportation, or any part thereof, as follows:

"The President in time of war is empowered, through the Secretary of War, to take possession and assume control of any system or systems of transportation, or any part thereof, and to utilize the same to the exclusion, as far as may be necessary, of all other traffic thereon, for the transfer or transportation of troops, war material and equipment, or for such other purposes connected with the emergency as may be needful or desirable."

(d) The proclamation of the President taking over the steam railroads, dated December 26, 1917, provides:

"Now, therefore, I, Woodrow Wilson, President of the United States, under and by virtue of the powers vested in me by the foregoing resolutions and statute, and by virtue of all other powers thereto me enabling, do hereby, through Newton D. Baker, Secretary of War, take possession and assume control at 12 o'clock noon on the 28th day of December, 1917, of each and every system of transportation and the appurtenances thereof located wholly or in part within the boundaries of the continental United States and consisting of railroads * * *"

"Nothing herein shall be construed as now affecting the possession, operation, and control of street electric passenger railways, including railways commonly called interurban, whether such railways be or be not owned or controlled by such railroad companies or systems. By subsequent order and proclamation, if and when it shall be found necessary or desirable, possession, control, or operation may be taken of all or any part of such street railway systems, including subways and tunnels."

(c) An act to provide for the operation of transportation systems under Federal control, with just compensation to the owners, etc., approved March 21, 1918.

(f) Army appropriation act, approved August 29, 1916, creating the Council of National Defense.

(g) Proclamation of the President establishing the War Industries Board, dated May 28, 1918, as follows:

"I hereby establish the War Industries Board as a separate administrative agency to act for me and under my direction. This is the board which was originally formed by and subsidiary to the Council of National Defense under the provisions of 'An act making appropriations for the support of the Army for the fiscal year ending June 30, 1917, and for other purposes,' approved August 29, 1916.

"The functions, duties, and powers of the War Industries Board, as outlined in my letter of March 4, 1918, to Bernard M. Baruch, Esq., its chairman, shall be and hereby are continued in full force and effect.

"(Signed) WOODROW WILSON."

(h) Letter dated March 4, 1918, from the President to Bernard M. Baruch, chairman, appointing Mr. Baruch as chairman of the War Industries Board.

(i) An act to authorize the President to provide housing for war needs, approved May 16, 1918:

"That the President, for the purposes of providing housing, local transportation, and other general community utilities for such industrial workers as are engaged in arsenals and navy yards of the United States and in industries connected with and essential to the national defense, and their families, and also employees of the United States whose duties require them to reside in the District of Columbia, and whose services are essential to war needs, and their families, only during the continuation of the existing war, is hereby authorized and empowered within the limits of the amounts herein authorized—

"(a) To purchase, acquire by lease, construct, requisition, or acquire by condemnation or by gift such houses, buildings, furnishings, improvements, local transportation, and other general community utilities and parts thereof as he may determine to be necessary for the proper conduct of the existing war."

"(d) To aid in providing, equipping, managing, and maintaining houses, buildings, improvements, local transportation, and other general community utilities by loan or otherwise to such person or persons and upon such terms and conditions as he may determine: *Provided*, That no loan shall be made at a less rate of interest than 5 per cent per annum, and such loan shall be properly secured by lien, mortgage, or otherwise: *And provided further*, That no loan shall be made and no house or money given under this act to any person not an American citizen."

"(i) An act making appropriations to supply urgent deficiencies in appropriations for the Military and Naval Establishments on account of war expenses for the fiscal year ending June 30, 1917, and for other purposes, approved June 15, 1917, authorizes and empowers the President—

"(d) To requisition and take over for use or operation by the United States any plant, or any part thereof without taking possession of the entire plant, whether the United States has or has not any contract or agreement with the owner or occupier of such plant."

"The word 'plant' shall include any factory, workshop, warehouse, engine works, buildings used for manufacture, assembling, construction, or any process

ess; any shipyard or dockyard and discharging terminal or other facilities connected therewith."

This act was subsequently amended to specifically give the President the power to take over electric railways, as follows:

(k) "An act to amend the emergency shipping fund provisions of the urgent deficiency appropriation act, approved June 15, 1917, so as to empower the President and his designated agents to take over certain transportation systems for the transportation of shipyard and plant employees, and for other purposes," approved April 22, 1918. Under this amendment the President is given power—

"(f) To take possession of, lease or assume control of, any street railroad, interurban railroad, or part thereof, wherever operated, and all cars, appurtenances, and franchises, or parts thereof, commonly used in connection with the operation thereof, necessary for the transfer and transportation of employees of shipyards or plants engaged or that may hereafter be engaged in the construction of ships or equipment therefor for the United States. * * *

"The President may exercise the power and authority hereby vested in him through the several departments of the Government, and through such agency or agencies as he shall determine from time to time."

(l) The act authorizing the President to coordinate or consolidate executive bureaus, agencies, and offices, and for other purposes, in the interest of economy and the more efficient concentration of the Government, commonly known as the "Overman Act," approved May 20, 1918, confers power upon the President to make such redistribution of functions among executive agencies as he may deem necessary whenever any functions, duties, and powers hitherto by law conferred upon any executive department, bureau, agent officer, or agencies in his judgment shall seem best fitted to carry out the purpose of this act.

IV. We submit that under the powers conferred in the acts above set forth Congress has conferred upon the President full and complete power and authority to assume control of the electric railways of this country. The greater power includes the less. The power to assume control may be entire control or a limited control, and if for the purposes of the war the only control that is necessary, as we contend, is to bring about increased revenue through an increased rate of fare, there is ample authority for the President to exercise control over these electric railways to the extent only of regulating their rates of fare. The purpose of all the above legislation was to confer upon the President the authority to do whatever is necessary in the national defense so far as the transportation facilities of this country are concerned. If this purpose can be carried into effect by a control limited to the fixing of rates of fare, he undoubtedly under such legislation has such power.

We respectfully submit that this is all that is necessary to meet the present emergency and put these electric railways in condition to efficiently discharge their duties so essential to the Nation's welfare at this time. The exercise of this power to increase the rates of fare to meet the extraordinary increases in the cost of labor and material which have been brought upon them by the war may be exercised by the President through such instrumentality as he may designate.

Respectfully submitted.

WAR BOARD AMERICAN ELECTRIC RAILWAY ASSOCIATION.

By P. H. GADSDEN.

Concurred in by—

JAMES H. VAHEY,

*Counsel for the Amalgamated Association of
Street and Electric Railway Employees of America.*

AMERICAN STAINLESS STEEL CO.,

Pittsburgh, Pa., September 13, 1918.

Hon. F. M. SIMMONS,

United States Senator, Washington, D. C.

MY DEAR SENATOR: I wish to thank you for the courtesies extended to me when I appeared before your Committee on Finance in behalf of a provision in the revenue bill exempting corporations from taxation on moneys given to charities, etc. I am inclosing herewith a statement on this subject, in which I have endeavored to answer the questions raised by certain members of your committee.

I trust you may be able to see your way clear to favor this provision.

Very truly, yours,

JAMES W. KINNEAR.

PITTSBURGH, PA., *September 13, 1918.*

To the MEMBERS OF THE COMMITTEE ON FINANCE,

Washington, D. C.

GENTLEMEN: You were kind enough to give me a few minutes before your committee on Tuesday last in behalf of exempting corporations from taxation on money given for religious, charitable, and educational purposes to 5 per cent of the net income of the corporation.

I desire in a few words to reply to the two objections raised by members of your committee to the insertion of such a provision in the new revenue bill, and would ask that this paper be filed in connection with my remarks made before the committee on Tuesday, September 10.

The objections were as follows:

The first objection was that the board of directors as a rule make such subscriptions for their corporations; that this is illegal and your committee would not insert a provision in the revenue bill which would seem to approve an illegal procedure.

In answer we would say if the stockholders in a legal manner approved the subscriptions or at their annual meeting authorized the board of directors to distribute a certain percentage of the net profit to charities, etc., it would not be an illegal procedure, and the provision in the bill should only exempt corporation subscriptions for charitable, educational, and religious purposes when the same are legally made.

Such a provision would have the effect of correcting all illegal methods of making corporation subscriptions to charities, etc.

The second objection was that even if the corporation subscriptions were approved or authorized by the stockholders their approval would be in a way coercive upon some stockholders who might not wish to make such subscriptions, but would do so rather than enter an objection.

This objection is weak, and there is a complete answer to it as follows: The stockholders are fully protected under the law; and if they ignore or refuse to invoke such protection, they alone are responsible.

The Senator raising this objection may have had the impression that a majority vote of the stockholders would be sufficient to legalize such a subscription; but this being a distribution of funds out of the ordinary line of business of the corporation, it would undoubtedly require the unanimous vote of the stockholders to approve or authorize such a subscription.

Why, then, should your committee feel called upon to protect the stockholders of a corporation who have it within their power to protect themselves?

To say that the large stockholders of a corporation as a rule coerce the small stockholders into giving to certain charities in which the former are specially interested is not true. Such a statement belittles and misjudges the big-hearted, generous business men who are running the corporations of this country and who keep its business pulsations throbbing from the Atlantic to the Pacific.

There are many reasons for exempting corporations from taxation on moneys legally given for religious, educational, and charitable purposes up to 5 per cent of their net income. Some of these reasons are as follows:

1. It is manifestly unfair to tax money given for public purposes of this kind when the country depends upon the public to finance so many public benefactions in connection with the war. All legislation should tend to increase public benevolences rather than diminish them.

2. It is frequently just as necessary for a corporation to give to the religious, educational, and charitable institutions, especially in the vicinity of the works of the corporation, as it is to build sanitary houses for the workmen. The latter goes into the expense account, but money given for the former must be taxed, although it is just as necessary and vital to the success of the company as the latter.

3. Corporations are the great money makers of this country. They will give more easily and in larger amounts than individuals, and this is a distinct advantage to great public undertakings, where large sums are especially required.

4. As a rule the man of small means gives more in proportion than the man of large means, but where the corporations contribute the large and small stockholder gives in proportion to their holdings, and for this reason refusal to insert a provision exempting from taxation corporations' subscriptions in a way protects the large stockholder more than it does the small stockholder.

5. The corporations of this country have given millions of dollars during the past year to the great public religious, educational, and charitable undertakings in connection with the war in addition to paying their war tax. The revenue bill which you are now considering will greatly increase their tax, the insertion of a provision exempting them from taxation on money given to public benefactions would be a recognition by Congress of what these corporations have done as well as an encouragement to continue. It will mean far more to the public welfare than any tax you may secure on the funds given for public benefactions.

There is no legal or moral reason why corporations should not be permitted to give to public undertakings and be relieved of taxation up to a certain amount of such gifts. It is a great deal better to give the corporations an opportunity to voluntarily dispose of some of their profits in this way than to force the same into the Public Treasury by drastic tax measures.

The insertion of a provision in the pending revenue bill exempting corporations from taxation on moneys given to public charities, etc., will result in a wonderful increase in the corporation gifts during the coming year, and hereafter the corporations of our country will become a great factor in sustaining all public benefactions.

Your committee is respectfully urged to insert in the pending revenue bill a provision which will exempt corporations from taxation on all moneys given for charitable, educational, and religious purposes up to 5 per cent of their net income.

WILMINGTON, N. C., September 11, 1918.

Hon. F. M. SIMMONS,
United States Senate, Washington, D. C.

DEAR SENATOR: I am inclosing herewith copy of a resolution of the Council of the City of Wilmington relating to the pending revenue bill in the Congress, particularly that feature of the bill which provides for the levy of a tax upon State and municipal bonds or obligations or interest on such bonds.

The power of the Congress to levy the proposed tax on State and municipal securities, to my mind, has been settled adversely to the Congress in the following cases: *Pollock v. Farmers Loan & Trust Co.*, 157 U. S., 429, 654; same case on rehearing, 158 U. S., 601; *Farmers & Mechanics Savings Bank of Minneapolis*, 232 U. S., 516; *Brushaber v. Union Pacific R. R.*, 240 U. S., 1; *Stanton v. Baltic Mining Co.*, 240 U. S., 103; *Peck v. Lowe*, 38 Sup. Ct. Rep., 432.

To say the least, the cases cited certainly make the question of the power of the Congress a very doubtful one. Aside, however, from the legal question involved, and waiving that for the moment in response to the patriotism of the people in the present national emergency, it seems to me that it will be wrong in principle and of the most far-reaching and hurtful results for the Congress to levy a tax upon State or municipal securities or the income derived therefrom, since in the last analysis it will amount to levying a tax upon the States or the municipalities, as the price at which such securities may be sold in the market or the rate of interest which the States or municipalities may be required to pay will be determined with direct reference to the fact that such securities or the income derived therefrom is taxable. Not only this, but on long-term bonds the States and municipalities will continue to suffer the effects of this legislation long after the war shall have ended, the time of their suffering being when the securities are offered for sale.

There are certain works of necessity in every State and in large numbers of municipalities which can not be postponed because of the war; in fact, the General Government is vitally interested in the undertaking by the States and municipalities, and pushing to completion, of certain public utilities and facilities which are absolutely essential to the conduct of the war. This is particularly true as to many cities in or in the vicinity of which the Government has located industrial plants, training camps, etc. This situation applies particularly to my own city, where the location of two shipyards has made necessary the building of many homes to accommodate the workmen, and the city is under the necessity of extending water and sewerage and other facilities to such homes, as well as building streets and roads in the sections where such homes are constructed. But few cities in this day and time are able to do more out of their current income than to meet current expenses, so that additional utilities and facilities require the exercise of the borrowing power.

I know the many difficulties which have beset you in your important office as chairman of the Senate Finance Committee, but I have thought it not improper to write you this letter in connection with the revenue bill and in connection with the copy of the resolution inclosed.

I am sending a copy of this letter and a copy of the resolution to Chairman Kitchin of the Ways and Means Committee of the House.

With assurances of my continued regards, I beg to remain.

Respectfully,

ROBERT RUARK,
City Attorney.

WILMINGTON, N. C., September 11, 1918.

DEAR SIR: Inclosed I beg to hand you a copy of a resolution of the council of the city of Wilmington, N. C., having reference to the pending revenue bill in the Congress of the United States, particularly that portion thereof by which it is proposed to levy a tax upon State and municipal bonds or upon the income derived by way of interest from such bonds.

This is a subject of vital importance, and one which would seem to merit concerted action on the part of governing bodies of municipal corporations throughout the country. It is recognized that under present conditions municipal corporations should desist from undertaking any unnecessary expenditures, but there are many things in the way of public utilities and facilities which are no less necessities in time of war than in time of peace—in fact, the very existence of the war has put upon many municipalities the burden of providing or enlarging certain public utilities to meet the needs of increased populations due directly to war industry or activity.

If you approve the views and suggestions in the inclosed resolution, we suggest the adoption of a like resolution by your governing body, and that the same when adopted be forwarded to our Senators and Representatives in Congress.

The city of Wilmington is ready to cooperate with any other of the municipalities of the State in such further action as may be proper in this connection.

Very respectfully,

W. D. McCAIG,
Chairman Finance Committee.
ROBERT RUARK,
City Attorney.

RESOLUTION OF THE COUNCIL OF THE CITY OF WILMINGTON, N. C.

Whereas attention of this council has been directed to the revenue bill now pending before the Congress of the United States, and particularly that portion thereof which provides a tax upon State and municipal bonds, or income in the way of interest upon such bonds; and,

Whereas serious doubt exists as to the power of the Congress to levy a tax upon such bonds or the income derived therefrom; and,

Whereas the levy of the proposed tax upon such bonds will have the effect of greatly limiting the market for such bonds, or possibly make such bonds unmarketable within the legal rates of interest provided by the laws of the several States, thus practically destroying the ability of municipal corporations to exercise their borrowing power, no matter what purpose or how great the necessity for the exercise of such power; and,

Whereas in the prosecution of the war the Government of the United States has located in and near various cities industries and activities highly essential to the successful conduct of the war, as a result of which the population of such cities has been greatly increased, thereby necessitating the enlargement and extension of public utilities in such cities, in response to which demand many of such cities have already undertaken or now contemplate the expenditure of large sums of money in the interest of the health and safety of their inhabitants, and unless such cities are enabled to exercise their borrowing power such utilities must remain uncompleted or plans to undertake such must be abandoned: Therefore,

Resolved by this council, That the Senators and Representatives from the State of North Carolina in the Congress of the United States be respectfully requested to take such action with reference to the pending revenue bill as

will prevent any impairment of the value or marketability of municipal bonds, especially such bonds as may be issued for the purpose of raising money with which to provide public utilities and facilities designed to protect the health, comfort, and safety of inhabitants of such municipal corporations.

Resolved further, That the finance committee of this council and the city attorney of this city be and are hereby appointed a committee to bring the matters referred to in this resolution to the attention of our Senators and Representatives in Congress, and to invite such cooperation as may be deemed wise and proper on the part of other municipalities within the State of North Carolina.

Adopted at regular meeting held September 9, 1918.

THE NEW YORK CLIPPER,
New York, September 13, 1918.

Hon. F. M. SIMMONS,

Chairman Finance Committee of the Senate.

DEAR SIR: I was unable to be present at the hearing this week, before your committee, of the theatrical managers' delegation, and would like the privilege of submitting for your consideration the following phase pertaining to the proposed increase of tax on admissions (in the pending war-revenue bill) from 10 to 20 per cent:

To my mind such a step would be a grievous error, for the following reasons: The Government is deriving a large revenue from the theaters, under the present law, from the admissions to theaters. The public responded when called upon to pay an additional 10 per cent for its amusements not because it could afford it but chiefly because amusements, as furnished by the theaters, have been found a necessary diversion because of the horrors of war.

It is the common impression that because of the abnormal prosperity of this country the public can afford to pay more for its various pleasures, of which the theater is the principal one. This is an error.

I am not certain, but I believe that statistics will show that nearly, if not quite, 80 per cent of the breadwinners of this country are salaried persons. It is this big class that is the main support of the theaters, and this class receives the same pay to-day as it did before this war began. The artisan, the mechanic, the skilled laborer have been benefited and are given opportunity to-day to earn from two to five times as much as they earned before the war. But they form a small percentage of those who attend the theaters. If the theater is placed beyond the reach of the salaried man, who goes to a place of amusement once or twice a week, he will retrench. In place of going once or twice a week he will go once or twice a month, and while the tax will be double what he now pays, the Government will only receive half the revenue it does now, because the patron will only go once where he used to go four times.

With the decrease in attendance the Government would also receive less income tax from the managers, and the moral effect on the public deprived of the privilege of going frequently to the theater because of expense would be more baneful than most persons dream of.

England and Canada both contemplated raising the amusement tax, but reconsidered it. England at the outset of the war (1914) even intended to do away with the theatre entirely—for the duration of the war—on the ground of being a nonessential. The British Government soon discovered its error and declared the theater an essential.

If the theater is essential in England it is essential in the United States, for we have the same amusements. If the theater is essential it should be fostered—not crushed—and I venture to say that the theater would be crushed with a 20 per cent tax on admissions.

Many a theater is keeping open to-day and making little money. All of these, probably 50 per cent of the theaters in the country, would have to close if their attendance fell even 25 per cent, and the 20 per cent tax is more likely to cut theater attendance in half in the high-priced theaters and down to one-third or one-fourth (of their present business) in the lower-priced theaters.

And this because the salaried man is the mainstay of the theater, and the salaried man—in New York, for instance—receives the same money to-day that he did four years ago and works harder for it.

Respectfully, yours,

ERNEST C. WHITTON.

(The chairman laid before the committee, and has made a part of the record, a letter from the American Railway Express Co., which is here printed in full, as follows:)

AMERICAN RAILWAY EXPRESS CO.,
New York, September 20, 1918.

Hon. F. M. SIMMONS,

Chairman United States Senate Committee, Washington, D. C.

DEAR SIR: Referring to conference with you on the 18th, I take the liberty of presenting the matter to you in writing on behalf of the American Railway Express Co., which is a company organized and incorporated for the purpose of acting as the agent of the Director General of Railroads in transacting the express business of the country, and which, under appointment and contract with the Director General, is now and has been acting as such agent since July 1 last.

I call your attention to the language in subsections A and B of section 500 of H. R. 12863, page 80, which seeks to impose a tax of 3 per cent of the amount paid for transportation by freight and a tax of 1 cent for each 20 cents or fraction thereof for the amount paid for transportation by express for such transportation within the United States of property transported from a point without the United States to a point within the United States.

This language applies to shipments from foreign countries which come into the United States by sea at ports of import and also which come by rail from Canada and Mexico. So far as shipments by sea which come into ports of import the tax on part of the transportation charge accruing within the United States can be collected, but so far as shipments which come in by rail from Canada and Mexico on through billing it is impossible to assess and collect the tax on part of the charge accruing within the United States. This for the reason, speaking particularly of Canada, that practically all rates, both by freight and express, from points in Canada to points in the United States are through rates which do not break at the border, and there is no division of the through rate which will show the charge accruing within the United States.

It is therefore suggested that at the end of subsections A and B of section 500, right after the words "United States," the following be added: "*Provided, however,* Where the property is transported upon through billings from an adjacent foreign country to a point in the United States the tax shall be assessed and collected from the consignee on the entire charge from point of origin to destination," which will result in the tax being assessed and collected in the United States on the entire charge.

I am of the opinion that the United States Government has the legal right to assess and collect a tax in the United States on delivery of shipments upon the entire charge from a point in a foreign country to a point in the United States.

If, however, it should be considered of doubtful legality to do this, then I suggest that the situation can be cured by an increase in rates from points in foreign countries to points in the United States.

Yours, truly,

T. B. HARRISON.

The CHAIRMAN. This concludes the hearings for to-day, and the committee will now adjourn to meet on Monday morning at 10.30 o'clock.

(Thereupon at 1.45 o'clock p. m. the committee adjourned to meet at 10.30 o'clock a. m. on Monday, September 16, 1918.)

TO PROVIDE REVENUE FOR WAR PURPOSES.

MONDAY, SEPTEMBER 16, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10.20 o'clock a. m. in the committee room, Senate Office Building, Hon. F. M. Simmons presiding.

Present: Senators Simmons (chairman), Smith, Thomas, Robinson, Jones, Gerry, Nugent, Penrose, Lodge, McCumber, Smoot, Dillingham, and Townsend.

The committee resumed the consideration of the bill (H. R. 12863) "to provide revenue and for other purposes."

The CHAIRMAN. Representative French, from the State of Idaho, desires to be heard and the committee will give him this opportunity to do so.

STATEMENT OF HON. BURTON L. FRENCH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF IDAHO, ON SENATE BILL 4879.

Mr. FRENCH. Gentlemen, I want to ask the attention of the committee to Senate bill 4879, introduced by Senator Borah. The bill is as follows (reading):

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That from and after the passage of this act, in addition to all taxes paid under existing laws, there shall be levied, assessed, and collected a gross sales (or transaction) tax upon every purchaser within the United States, as follows:

First. One cent on each purchaser in a transaction aggregating an amount from 5 cents to \$99.99.

Second. Three cents on each purchaser in a transaction aggregating an amount from \$100 to \$499.99.

Third. Six cents on each purchaser in a transaction aggregating an amount from \$500 to \$999.99.

Fourth. Ten cents on the first \$1,000 and 5 cents on each additional thousand or part thereof on each purchaser in a transaction aggregating an amount from \$1,000 to \$9,999.99.

Fifth. Twenty cents on the first \$1,000 and 4 cents on each additional \$1,000 or part thereof on each purchaser in a transaction aggregating an amount from \$10,000 to \$49,999.99.

Sixth. One dollar on the first \$1,000 and 3 cents on each additional \$1,000 or part thereof on each purchaser in a transaction aggregating \$50,000 or more.

Provided, however, That there shall be exempt from the tax the following: The Federal Government; all State, county, city, and municipal governments; all Governments recognized as allies in the prosecution of the present war; all

enlisted men in the military or naval service of the United States, in uniform at the time of purchase, and all officers and enlisted men when within the United States and in uniform at the time of purchase, of the naval or military service of countries that are allied with the United States in the present war; the American Red Cross and other authorized relief organizations designated by the Secretary of the Treasury while making purchases for actual relief work under their direction; entertainments, fairs, socials, dances, or other amusements carried on to raise money for authorized war relief work where all of the proceeds collected are to go to such war relief.

SEC. 2. That the tax provided for herein shall be satisfied by each purchaser in the transactions to which the tax pertains by affixing a stamp to be known as a war-purchase stamp in the amount indicated to the thing purchased or by paying to the seller in the transaction a stamp or stamps equaling the required tax, and it shall be the duty of the purchaser to cancel the stamp used by writing his initials and date upon the same, or by such other manner as may by the Commissioner of Internal Revenue be prescribed.

SEC. 3. That the provisions of this act shall be administered under the immediate direction of the Secretary of the Treasury, but the President of the United States is further authorized to call upon the Postmaster General or any other officers of the Federal Government to cooperate in the administration of the same.

SEC. 4. That the Secretary of the Treasury, under such rules and regulations as he may prescribe, shall cause to be printed stamps in such denominations as will conveniently meet the conditions of the act and shall make such rules and regulations as may be consistent therewith.

SEC. 5. That war-purchase stamps shall be sold at United States post offices, branch post offices, and such other places as may be provided for under the rules and regulations of the Secretary of the Treasury.

SEC. 6. That the purchaser and the seller in every transaction are made responsible for any failure to affix and cancel a war-purchase stamp in the amount required in any transaction, and whoever as purchaser omits to attach to the thing purchased, or the receipt or other evidence of the thing purchased, or to surrender to the seller the stamp provided for in the transaction, shall be guilty of a misdemeanor, and for each offense shall be fined a sum not less than \$100 or imprisoned for a term not exceeding one year, or both, in the discretion of the court. Whoever as seller in a transaction completes the sale and omits to require a war-purchase stamp to the thing sold or surrendered to him, as the case may be, shall be deemed guilty of a misdemeanor, and for each offense shall be fined in a sum not less than \$50, or imprisoned for a term not exceeding six months, or both, in the discretion of the court. Any person who shall use a war-purchase stamp that has been canceled in a place where a war-purchase stamp is required to be used, or who shall counterfeit such stamp, or shall formulate any scheme or engage in any propaganda or publicity or agitation against the use of war-purchase stamps, as herein provided, shall be deemed guilty of a misdemeanor, and for such offense be fined in a sum not exceeding \$5,000, or imprisoned for a term not exceeding ten years, or both, in the discretion of the court.

Whoever as a seller in a transaction uses the payment of the tax provided for in this act by himself or his concern as a means of obtaining business by the payment of the same by him or his concern, and thereby relieving the purchaser of the intent of this act, will be deemed guilty of a misdemeanor, and for each purchase-transaction offense will be fined in a sum not less than \$100 and not exceeding \$500.

SEC. 7. That for a period of not less than thirty days prior to which the provisions of this act become effective the Secretary of the Treasury shall cause to be carried on throughout the United States, through the Bureau of Public Information and otherwise, a publicity campaign of education, and such campaign shall be deemed a sufficient notice to all persons touching the provisions of the act. The President of the United States shall by proclamation define the date when such campaign shall begin.

SEC. 8. That the term "sale" as herein used shall be held to mean any transaction in which commodities, services, or any things of value shall be exchanged for money or other commodities, services, or any things of value. The purchaser shall be understood to mean the parties or party to the transaction whose commodities, services, or any things of value aside from money, and when the transaction involves an exchange of commodities, services, or things of value, both

parties to the transaction shall be deemed purchasers to the extent of the whole transaction, less to the person receiving part consideration in money the amount of money that is received.

Mr. FRENCH. I now desire to present to the committee a telegram which I received on day before yesterday from Mr. C. A. Mariani, of Twin Falls, and Pocatello, Idaho, upon this measure. Mr. Mariani is the author of the bill and was called home on important business some days ago, after having come to Washington to present his idea to the Congress. In fact, I understand he was to have addressed your committee. Mr. Mariani's telegram is as follows [reading]:

TWIN FALLS, IDAHO, September 13, 1918.

Congressman BURTON L. FRENCH,

House of Representatives, Washington, D. C.:

In my name, in accordance with arrangements made with Chairman Simmons of the Senate Finance Committee, will you kindly appear before them Monday or Saturday of this week with the following testimony on Senate bill 4879:

Bill was created by me in Idaho at the instigation of no one and at the consideration of no special interests. It is a war measure, designed to produce large revenue, procuring same where it will do the least financial harm. I estimate that in retail purposes that if everyone in America, men, women, and children, average 4 purchases per day each (which would be a general average of 12 purchases to the family), under this tax the most the individual could pay would be \$12 per year, and the most the average family would pay would be \$36 per year. The clothing women wear, shoes, tobacco, patent medicine, candy, soft drink, picture shows, and club clauses alone of the House bill will very greatly exceed this amount of individual and total family taxation.

Under House bill there are too many who could escape their share of taxation. Under my bill every one of the hundred million residents of America and its possessions pays his share. This bill is more equitable than any form of taxation in existence in this or any other country at this time. My tax as proposed on retail, wholesale, manufacturing, and all other purchases other than individual consumers' purchases, averages 5½ cents per thousand dollars, and although it will produce an enormous amount of money, it is so small on individual sales that it is the only form of taxation that will not be passed along to the consumer, because on retail or wholesale manufacturer, and so forth, it is so infinitesimally small in percentage that it is lost.

Publicity campaign feature would practically compel American purchaser to combine sales, thereby reducing amount of tax he would pay. Every other tax is definite on amount on each item with no escape. The individual under my bill can daily escape tax by compounding sales into one purchase. Five-cent stores and some merchants making bulk sales under 25 cents complain that this bill is a hardship. The administration of the bill will permit the use of transfer systems which will combine all an individual's shopping transactions in a department or 5 or 10 cent store or similar business at one time into one purchase, therefore one tax under this bill.

For the benefit of the very poor the revenue department could authorize to be issued by dealers weekly milk, ice, or fresh vegetable cards which would carry 1-cent tax each per week.

This bill will stabilize business as many merchants such as restaurants, etc., will be able to count a definite patronage owing to the number of meal tickets, ice cards, vegetable cards, and milk cards that are out still unused. The waste saved in these two lines of business alone would justify passage of this bill. If publicity feature is carried out universally in very extensive campaigns. The individual consumer on reduced prices on goods received by combined purchases and in time saved in making few combined against multitude of individual purchases in many instances will repay the individual the total amount of taxation paid out by him under this bill in a year. In other words, this bill is designed to wipe out an existing social evil—the cost of doing business of the individual.

I estimate that this bill will produce 4 cents a day from every individual in America on individual purchases which is \$1,200,000,000 a year in taxes. I further declare that the American individual wastes more than 4 cents per day in his unbusinesslike mode of purchasing in existence to-day.

The retail, wholesale, manufacturing, labor hiring, and miscellaneous forms of purchasing, outside of the individual's purchases, will produce the big bulk of taxes claimed for this bill.

Notice the man-saving feature of the bill. The labor that can be saved by combined purchases in the retail, wholesale, jobbing, and manufacturing business. Labor can be saved to the extent of the amount of additional men required under the 18 to 45 draft law.

A new argument that is uppermost in the minds of all merchants to-day is that under the House bill as proposed the impression prevails that the Government is killing the goose that lays the golden egg if we are going to raise twice the amount this year by taxation that we did under last year's bill. The American merchant has either got to do a much increased business or he has got to take the increased tax out of the consumer by fabulous prices. A woman goes into a store under the new bill and prices a dress; the merchant says \$45. She says, I'll take it. The merchant says but there is a \$9 tax on it. This makes it cost too much and the merchant is out that business. A person goes in to buy a 5-cent glass of soda water and under House bill, he must pay a 2-cent tax, but the merchant is not going to charge a 2-cent tax, he is going to charge a 100 per cent tax or 10 cents a drink for the soda. This is going to cut down the business where the 1-cent tax on individual purchases will not effect the volume of the business at all.

The only real argument made against this bill of mine is that it is unhandy, which I admit, but these are war times and it is also unhandy for 5,000,000 men to leave their families and go to France.

But this bill of mine will not reduce the volume of business. Under the House bill many picture shows will close, and this is especially harmful to business in small communities where the family drives into town to a picture show. They also do a little town shopping which makes business there better. I have seen many towns where the one little form of amusement device was closed and in every instance business was dead. The publicity being sent out by the National Council of Defense and a number of the orders issued by the War Industries Board on curtailment are having the effect of generally reducing business, are having too much of an effect toward the absolute curtailment of business. War industries, manufacturers, food producers, food brokers and jobbers, wholesalers, and even the farmers are all making excessive profits, but the general American retail merchant, the very backbone of American industry, is not averaging 7 per cent per annum on his investment, and many of them are going out of business. In Idaho there is not a retail merchant that can not be bought out for invoice. In the same State a few manufacturers, all farms, all dairy products concerns, in fact, all big business, is in the most prosperous condition, and yet the House bill is designed to hand it to the retail merchant harder than anyone else. I estimate under the House bill business continuing on the basis of last year, that the average American family will pay an \$87 commodity tax. Under that bill this is going to greatly reduce the output of the retail dealer.

The schedule of taxes presented in this bill is only tentative. What we are fighting for is the principle of the taxation. The penalty clauses of the bill automatically make every seller in America a compulsory agent of the Internal Revenue Department.

This is the first revenue bill where the responsibility for the payment of the tax is put where it was intended to be put, namely, on the purchaser which in reality is the intention of every tax bill, but very seldom carried out.

Line 5, page 5, of bill provides penalty, which penalty prevents the use of this bill for advertising purposes and again puts the responsibility back on the purchase.

The sentimental, patriotic features of this bill put every American actively in the service. Every time he makes a purchase he is paying one-thirteenth of a ration of one of the boys over there, and don't forget because it is a cent at a time no one will consider it a hardship.

In conclusion, this bill is only presented to be used as an amendment to take the place of the Ways and Means Committee bill on commodity taxes and has no intention of replacing the income tax, excess-profits tax, or surtax features of the House bill.

I am of the opinion that any man that wants over 6 per cent net on his investment until after this war is won is a pro-German and should be shot up against a stone wall.

C. A. MARIANI

Mr. FRENCH. Gentlemen, the statement of Mr. Mariani is so complete that there is little I need to add. By way of outlining the bill, I will say that it provides for a tax upon gross sales or transactions. You will notice in the first section of the bill that it provides that 1 cent shall be taxed upon the purchaser in a transaction aggregating in amount from 5 cents to \$99.99; second, 3 cents on each purchaser in a transaction aggregating in amount from \$100 to \$499.99; third, 6 cents on each purchaser in a transaction aggregating in amount from \$500 to \$999.99; fourth, 10 cents on the first \$1,000, and 5 cents on each additional \$1,000 or part thereof on each purchaser in a transaction aggregating in amount from \$1,000 to \$9,999.99; 20 cents on the first \$1,000 and 4 cents on each additional \$1,000 or fraction thereof up to \$49,999.99; \$1 on the first \$1,000 and 3 cents on each additional \$1,000 aggregating \$50,000 or more.

Probably I should say, in addition to this, that the tax is to be paid by the purchaser in each transaction, but the purchaser and the seller are both made responsible for the payment of the tax.

It is provided in the bill that there shall be stamps issued which shall be in the possession of the purchaser, and these stamps shall be placed upon the commodity purchased, on the package, or shall be canceled by initialing or in some way provided by the responsible officers in carrying out the provisions of the law.

The CHAIRMAN. You say the stamps must be in the possession of the purchaser?

Mr. FRENCH. Of the purchaser; yes.

The CHAIRMAN. Then when I go into a store I have to take stamps along with me?

Mr. FRENCH. You would either have to take stamps, or else the Revenue Department would need to provide a place where stamps could be acquired within the store.

Senator PENROSE. Has any rough estimate been made as to the amount of revenue that would come under this bill as it stands now?

Mr. FRENCH. I was going to speak of that first. Mr. Mariani is the author of the bill in principle. He is a resident of Idaho, a man engaged in the wholesale business, and himself personally interested, I believe largely as a traveling salesman. He wanted it distinctly understood that the bill as proposed is his own idea, that it is not backed by any organization or by any interest. He wanted that statement made so that you can understand how disinterested he is in urging it upon Congress.

He has estimated that each family will purchase possibly on an average 12 times during the day; that transactions of that character, under class 1 of the bill, would provide not less than about one billion and a quarter of dollars. He said that it is very hard to get a line on the number of purchases that are made in the country. Of course, the transactions under the different subdivisions—2, 3, etc.—would be hard to estimate. But as the tax there is larger and increasingly larger, necessarily a vast amount of money would be produced. Mr. Mariani thinks that several billion dollars would be produced by the bill. He does not propose that the measure shall be a substitute for the entire revenue bill, nor for the feature of the bill providing for taxation upon incomes, war profits, excess profits, etc., but rather for the taxes provided through other features of the bill as it has been presented to the House.

Senator TOWNSEND. To start with, let me ask you this: Supposing a woman goes into a grocery store this morning to buy a dozen articles—different items. Each one of those is to be taxed, or the total bill?

Mr. FRENCH. The idea is that the total bill is to be taxed and the author's idea still further is this, that with respect to certain commodities that must be bought from day to day—such as ice, milk, and boarding-house tickets, etc.—an arrangement could be made for a ticket to be sold, say, by the week or by the month, whatever would seem most calculated to produce the most equitable condition upon the part of the purchasers who are compelled to purchase certain commodities in a small way.

Senator SMOOT. Congressman French, I had Mr. Mariani in my office for some time before this bill was printed, and I called his attention to the almost absurdities of the bill the way it is drawn. For instance, you take the first tax imposed—1 cent on each purchaser in a transaction aggregating in amount from 5 cents to \$99.99. In other words, that tax is 20 per cent on a 5-cent purchase, and one one-thousandth of 1 per cent on a \$99.99 purchase. Do you think the American people would stand that?

Mr. FRENCH. Let me come to that in just a little bit.

Senator SMOOT. I could go right along with the others, and show that the small purchaser under this gets it "in the neck," so to speak, and there is a difference between 20 per cent on the one and one one-thousandths of 1 per cent on the other.

Mr. French. Probably, since the question is raised, I would just as well speak of that point right now.

Senator SMOOT. I thought he was going to change his bill.

Mr. FRENCH. Mr. Mariani is engaged in a business that brings him into contact with the retailer and with the wholesaler. His estimate is this, that while, of course, there is that apparent hardship imposed upon the person who purchases a 5-cent article compared with the person who purchases a suit of clothes that costs less than \$100, the tax being the same, the opportunity for combining purchases made by the purchaser is such that there will be effected a saving in doing business vastly more than the tax itself imposes.

Senator SMOOT. How do you combine the purchase of clothes with the purchase of a cigar?

Mr. FRENCH. The idea is this, to-day people go to stores frequently, repeatedly, the housewife and the children, especially in towns and cities, and will make several or many visits to the local merchants to make the purchases. If the housewife made, under this bill, the same number of purchases, she would need to pay 1 cent every time she made a purchase.

Senator SMOOT. She could not purchase the cigar at the clothing store.

Mr. FRENCH. No; but very generally she would be compelled to combine where possible, and there would be an inducement offered in the measure, for her to combine her purchases, so that in the morning when she purchased her groceries, she would purchase all the staple articles she would need possibly for several days or for a week, and pay 1 cent in the way of a tax in making the transaction.

Senator McCUMBER. How would you arrange a stamp tax on a sale over the phone?

Mr. FRENCH. That will need to be worked out.

Senator McCUMBER. That would compel a housewife in this city to hang on to the cowcatcher of the car in order to get a ride downtown to make a purchase. She has to use the phone for it.

Mr. FRENCH. I do not doubt that that matter could be worked out through the sales slips maintained by the merchant.

Senator McCUMBER. It could easily be worked out by having the seller attach the stamps and charge them.

Mr. FRENCH. Yes; that could be done. A seller could attach the stamps and they could be charged. Of course, the theory of the tax is that the tax shall be paid by the purchaser.

Senator McCUMBER. There is another question I want to ask right there. I notice that you have exemptions. How are you going to have exemptions for taxes when the stamps are attached on each little purchase, and then you make an exemption of the taxes paid the Government, etc., from the general taxes?

Mr. FRENCH. The exemptions in the bill touch State, city, and municipal governments, certain persons and employees in the prosecution of the war, the American Red Cross, etc.

Senator McCUMBER. What I mean is this, you say there shall be exempt from the tax the following: The Federal Government and all State, county, city, and municipal government taxes.

Senator TOWNSEND. Those are not taxed, are they? Those are goods purchased.

Mr. FRENCH. Purchases that may be made for them are exempt from bearing the tax.

Senator ROBINSON. Why is the tax levied on the purchaser rather than the seller? Would it not be far more convenient to require the seller to attach the stamps and to provide the stamps?

Mr. FRENCH. Let me just finish up first the question that was asked by Senator Smoot, and then I shall come to that point, the question of the tax being large upon the small purchaser in comparison with the tax paid by the large purchaser. In the first place, it is believed that the small purchaser would become accustomed to combining his purchases, so that in that way he would save a vast deal.

Senator ROBINSON. Let me ask you a question there. Unless the authority to combine is implied in the word "aggregating," I do not see, from a casual reading of the bill, where a transaction might not be construed to be each separate sale, and thus the purchaser be prevented from combining the sales.

Mr. FRENCH. If there is any question as to the language meaning what it is intended to mean, undoubtedly it could be whipped into shape. But carrying out still further the idea that I suggested a moment ago with regard to the purchaser saving by combining his purchases, I would say this, the housewife who is in the habit of going 8 or 10 or a dozen times to the store or sending her children to make certain purchases would combine her sales. Instead of purchasing maybe 30 or 50 times in the course of the month she would purchase a quarter of that number of times, or maybe less than that. What would be the first effect of a community purchasing in such quantities as to reduce the number of sales from a quarter to a sixth the number of sales, the volume of business still remaining the same? Of course, it would be obvious that the merchant would dispense with a clerk;

he would dispense with a deliveryman; he would dispense, possibly, with a bookkeeper. Maybe, if his store were large enough, it would give him the opportunity of dispensing with several employees that he has. The merchant could sell for enough less to more than make up for the tax, and in that way would attain another thing that I want to come to a little later on under this bill. There would be a saving of man power, which is essentially needed at this time in the United States.

Senator ROBINSON. Yes; and incidentally expense to the seller. And I again ask, if that is the case, why the tax should not be imposed on the seller instead of the purchaser?

Mr. FRENCH. I am just coming to that.

Senator PENROSE. Was this proposition submitted to the House committee?

Mr. FRENCH. It was not submitted to the House committee until after the hearings had been closed and the bill was practically prepared. After that Mr. Mariani appeared before individual members of the House committee to present it to them. They felt that it was illogical for them to consider a proposition that they had not had hearings upon that was of such vast apparent importance as this, perhaps, and felt that it was not the time for them to consider it.

Senator PENROSE. I think the proposition was formally submitted in the Ways and Means Committee by one of the members and voted down unanimously as affecting too many voters.

Mr. FRENCH. I think the proposition that was submitted differs from this in this, that the gross-sales tax submitted had to do with each particular sale and not with combined sales. I can see how if the purchaser, every time he purchases one little item, whether it is a box of matches, a bottle of extract, or what not, were taxed, it would be a tremendous tax piled up on the small producer, probably almost as great a tax as would be piled up upon the wealthy producer, but if a combination can be made in purchasing, as is proposed in this bill, there would not exist that inequality.

Senator JONES. Speaking of the things which would probably be dispensed with if this bill were enacted, would it not have a tendency to dispense with all stores except the big department stores, where a person could go in and purchase dry goods and groceries and boots and shoes at one place and have but one transaction?

Mr. FRENCH. I think that the fact that the tax is so small upon the purchaser, plus the other fact that the people do not care to invest so large an amount of money in household goods, would probably operate effectively to prevent that very condition from arising.

Now, going to the question raised by the Senator from Arkansas, why not let the seller pay the tax and charge it on to the purchaser? The reason is this, we have that provision under the present law. For instance, you go into a drug store and buy a package of tooth paste. The tax on that, as I understand it, is 2 per cent upon the value. If that package of tooth paste has a value of 25 cents, the tax would be a quarter of a cent. The druggist, though, does not charge you a quarter of a cent; he does not charge you 1 cent, but he charges you 5 cents or 10 cents, and if you raise a complaint about it he says, "I have got to pay the Federal Government a tax upon this package." He takes it for granted that the purchaser will not know that the tax is a quarter of a cent, and not the 5 or the 10 cents.

Senator ROBINSON. You have assumed to restate my question and embrace within it elements that were not in the question I asked. You assumed I implied the obligation upon the part of the seller to pass the tax on to the purchaser. I did not do that. I expressly asked you the question, since, according to your own statement, this scheme would result in a great saving to the seller, why would it not be proper to let the seller pay the tax? I did not ask you anything about charging it on.

Mr. FRENCH. The point that the Senator raises, it seems to me, is one that must be met as I have met it. I can not see how you can avoid it being charged on to the purchaser.

Senator ROBINSON. For the simple reason that the seller has, by being allowed to combine these sales, avoided considerable expense. He has discharged a lot of his clerks.

Senator McCUMBER. But the purchaser does not have to pay any more. They will buy the small packages, separately. Therefore he would be at the same expense, and his tax would be heavier.

Mr. FRENCH. It seems to me that if you require the seller to pay the tax, the seller, even if he does not have to put the stamp upon the particular commodity, as he does now upon the package of tooth-paste that I used as an illustration, the seller would nevertheless gradually raise the price of his commodities so as to take care of this tax, and thereby pass it on to the purchaser.

Senator McCUMBER. One of the primary purposes, then, is to force the combination sales?

Mr. FRENCH. Yes; that is one—one of the most important.

Senator McCUMBER. And as suggested by the Senator from New Mexico, that would encourage purchases from houses that had a great variety of articles to sell, in other words, department stores, and would discourage purchases from stores that are dealing in specific commodities, like groceries, dry goods, and other businesses of that sort.

Mr. FRENCH. If people were willing to purchase commodities in such great quantities, and tie up their money in that way, there might be a good deal in that suggestion. I do not fear it at all.

Senator McCUMBER. And if the tax were made high enough, if they were resorted to as one of the principal means of taxation, it would result in the concentration of all the selling business of the country in the form of department stores, would it not?

Mr. FRENCH. I personally do not catch the weight of that suggestion as emphatically as the Senator does. It seems to me it would not.

Senator McCUMBER. I say, if that tax got high enough to induce a purchaser to avoid the tax by combining the sales—that is, to avoid a number of transactions, and pay a tax a number of times, he would go to a department store where he could get all his things in the one place, and pay one tax, rather than go to the other stores?

Mr. FRENCH. Oh, undoubtedly, if the tax were made high enough. It seems to me, though, that with the tax of 1 cent on a transaction, that is not high enough to induce a purchaser to do that.

Senator McCUMBER. I think the bill is simply impossible, as suggested by the Senator from Utah.

Senator PENROSE. I would like to ask the witness this question: Would not the rider on a trolley car, when he would pay his five cents, have to pay an additional cent for his fare under this bill?

Mr. FRENCH. I suppose he would, under this bill.

Senator PENROSE. That would be a very heavy burden on the traveling public.

Mr. FRENCH. Yes; unless another system were worked out similar to that already suggested, by which the tickets, even though no reduction were made in the tickets, could be furnished to the purchaser, and if the language of the bill is not broad enough to comprehend that, of course, it can be readily amended so that it would be.

Speaking further, though, upon the tax being paid by the purchaser instead of by the seller, under the present law we have a tax that is paid by the seller on, say, the elements that enter into a soda. As I understand it, the cost to the dealer in the commodities that enter into a soda is less than 2 cents, not to exceed 2 cents, per glass. Yet the price of the soda has gone from 5 cents to 10 cents, and the theory is that it is because of the tax, and the excuse made by the dealer to the purchaser is that it is because of the tax.

Senator THOMAS. It is the extra labor of mixing the drink.

Mr. FRENCH. You even go out here to the ball park, in this city, and where you have been paying 75 cents to the baseball company for your ticket you now pay 75 cents plus the tax of 8 cents plus something more. The ball club does not limit the ticket to that amount. It charges you 2 cents extra; or, in other words, 75 cents plus 8 cents and 2 cents, a total of 85 cents. Of course, the extra 2 cents you pay does not go to the Government. It is not collected as a tax, but probably from the standpoint of convenience. So on a thousand persons who go in at the gate the ball club collects an additional \$20, made possible because of the fact that the tax is paid in that way.

There is another point that I wanted to call attention to. The tax is self-enforcing. The burden of paying the tax is upon the purchaser. But in the bill, as you have noticed, there is a provision that the seller shall also be under penalty providing he does not see to it that the tax has been paid.

Senator ROBINSON. He will raise the price to the purchaser for supervising the payment of his tax.

Mr. FRENCH. We have that same principle, of course. This is not a new principle. If you go into a bank to make a note the bank is required, of course, to see to it that certain stamps are placed upon that note, just as the maker is.

Senator ROBINSON. If the business concern is penalized for failure of some one else to pay the tax, the obligation becomes so onerous upon the business concern that it would have to have persons specially charged with the duty of supervising the payment of that tax. A respectable business concern that was penalized for the failure of some one else to discharge a duty would be compelled to have persons to see that the duty was performed, and that would add an additional expense to the purchaser.

Mr. FRENCH. There is another point I wanted to speak of in connection with the bill. It is urged that the system is unhandy. So far as that is concerned, the paying for goods is unhandy, the collection for goods is unhandy, and yet business could not proceed unless we

had the transactions. But the payment of any tax is unhandy, and I suppose that the question of loyalty and patriotism would itself need to be relied upon in this country in overcoming the objection that this or any other tax is unhandy.

Senator JONES. The purpose of this bill is to have a universal consumption tax levied, is it not?

Mr. FRENCH. It would be a tax that would reach everybody; that nobody could escape; that it would seem would be simple of enforcement; that would raise a vast amount of money, and also that would tend to conserve the man power of the country by driving the purchasers to make their purchases in bulk rather than in many items. It does not take the place of income tax, excess profits, and war-profits taxes.

Another objection is—and that is suggested by Senator Jones—that it is a consumption tax, and therefore, I suppose, carrying out the idea of the Senator, it would fall heavily upon the small purchaser in relation to the large purchaser. But there will be, in my judgment, a tremendous saving on account of the combining of purchases, which will offset the tax.

Senator JONES. This would be an income tax, too, would it not? All taxes are taxes upon incomes in one sense of the term, the broad sense of the term, and this would simply be a tax upon the small incomes?

Mr. FRENCH. You could possibly phrase it that way. It is a tax upon expenditures.

Senator TOWNSEND. Has this principle been employed in any other country, do you know?

Mr. FRENCH. I think it has not. The same question I raised a little bit ago—about compelling or inducing the small purchaser from the retail store to combine his purchases—would also apply to the retailers with regard to the purchases that they make from the wholesalers. In that way the wholesaler would in turn be able to dispense with help. Instead—for instance, in the city in which a business is located—of wagons supplying retailers being required to make four or five or half a dozen trips to a retail house during a day, the wagons would make possibly one trip or a few trips during the week. And, again, a saving would be made there in man power. The idea can be carried on, then, to the business with the larger wholesaler and the smaller wholesaler located throughout the country.

Unless there is something further that some Member would like to ask, that is all I have to say. I regret very much that Mr. Mariani was called home, so that he could not have appeared in person to have explained the idea to the gentlemen of the committee.

Senator SMOOR. I will assure the gentleman that he has explained it just as well as Mr. Mariani explained it to me.

Senator TOWNSEND. I think it is rather a serious matter myself, because some of the very strong men of the country are talking about it. But they have met, just as the Senators have here, the same objections which they were not able to overcome. I could see where, by relieving the numerous taxes we provide in the bill, by putting some such system in effect, it would be a good thing; but nobody has been able to explain to me how it can work. If you take a per cent tax on purchases, it might be possible.

Senator ROBINSON. It would be unconscionable to make the man who is unable to buy a considerable amount pay the great burden of these taxes. I think it would be positively reprehensible to say that the poor woman, who earns her living, and can spend only 50 cents or a dollar a day, shall pay more than the man who is able to make large purchases. I think that would be absolutely unconscionable. As far as I am concerned, I could not consider that.

The CHAIRMAN. Let me suggest that we are simply hearing these gentlemen now. We do not want to enter into a discussion of the merits of the bill at this time.

Senator PENROSE. I would like to ask the Congressman one question. This bill was introduced by Senator Borah, who does not appear. Is the committee to understand that Mr. Borah advocates this measure, or simply introduced it by request?

Mr. FRENCH. I would not assume to speak for Senator Borah. I had gone over this matter so carefully with Mr. Mariani that when he was called away on account of his business he asked if I would not come before the committee and make a statement for him, and also place with the committee certain data and a telegram he has sent, and that is my business in coming. In no way do I suggest Senator Borah's position on the bill.

Senator LODGE. There is nothing to indicate that it was introduced by request.

Senator ROBINSON. I heard the statement of Senator Borah when he introduced the bill, and he suggested that it was prepared by another man, and he did not assume responsibility for all of its provisions.

The CHAIRMAN. Did you introduce this bill in the House?

Mr. FRENCH. My colleague, Mr. Smith of Idaho, introduced the bill in the House after the hearings had been concluded in the Ways and Means Committee and the bill practically completed.

The CHAIRMAN. Mr. Mariani is the gentleman who came with you to see me?

Mr. FRENCH. Yes; Senator Simmons.

Senator PENROSE. Will this bill be offered as an amendment on the floor of the House?

Mr. FRENCH. I do not know.

The CHAIRMAN. Is it your purpose to offer it?

Mr. FRENCH. It is not my purpose to offer it. The author of the bill on the House side, the gentleman who introduced it, is Representative Smith. Of course, it would be for him to determine whether or not it would be advisable to present the bill as an amendment.

I thank the gentlemen of the committee for their attention.

The CHAIRMAN. Mr. Pound, we will be pleased to hear you now.

MUSICAL INSTRUMENTS.

STATEMENT OF MR. GEORGE W. POUND, GENERAL COUNSEL AND MANAGER MUSIC INDUSTRIES CHAMBER OF COMMERCE, NEW YORK.

Mr. POUND. Mr. Chairman and gentlemen, I desire to address myself to sections 900, 909, and 910, section 900 being the excise tax upon musical instruments, and sections 909 and 910 the new floor tax.

Senator PENROSE. What interests do you represent?

Mr. POUND. I am general counsel of the Music Industries Chamber of Commerce, which represents the musical-instrument industry of America, with the exception of the phonograph interests, with which we have no concern.

The CHAIRMAN. What page are those sections on?

Mr. POUND. The floor tax is page 137, and the other tax is page 127 of the House bill.

In the present act, of October, 1917, the corresponding section to section 900 is section 600, subdivision B. We were there taxed in all respects the same as here, except that the words "pianos or pipe organs" were not included, and the tax was 3 per cent instead of 10.

I will not attempt to discuss the amount of the tax here, but confine myself purely to the language of the section.

We have adjusted our business, after some considerable difficulty, to meet the wording of the present law, "piano players, phonographs," etc. Many of our concerns are manufacturers both of pianos and the various forms of pianos and of phonographs.

Senator GERRY. I thought you said you did not represent the phonographs.

Mr. POUND. No; I do not represent the phonograph industry as such in its entirety, and for the purposes of this argument I am not speaking of that end of it.

Senator THOMAS. They can speak for themselves.

Mr. POUND. So far as I know, there is no country in the world which taxes the ordinary or straight piano, what we generally term in our industry as the poor man's music.

Senator THOMAS. There is one in an adjoining apartment to mine that I would like to tax.

Mr. POUND. Probably that would be the individual, rather than the instrument.

Senator THOMAS. I do not know whether it is straight or upright.

Mr. POUND. The pipe organ, so far as I know, is not taxed in any country. It was supposed to have been taxed in Canada, but I have a communication here which says that by section 6 of the special war-revenue act of 1916 on musical instruments, the war excise tax is only payable upon pianos and organs in respect to the player action installed therein or attached thereto, and that is substantially the view which has been taken of the present act. It is the ruling of the Internal Revenue Department here. In other words, the simple, straight piano is not of itself taxed. It is taxed only when it gets into its playing form, the playing mechanism.

The pipe-organ business in this country to-day is substantially out of business, with the exception of some few hang-over orders, some few church orders. This tax upon pipe organs would be substantially a tax upon the churches of the country. Such places as public halls or places of public amusement are not buying pipe organs. They use the other forms of instruments, mostly, and at the present time are largely using orchestras. The substantial, and almost without exception, the entire pipe-organ business of the country is now that which is being furnished to churches. The units of value are very large of the pipe organs, the ordinary church pipe organ running from \$10,000 up, and a tax of 10 per cent on them would be absolutely prohibitory. The pipe-organ business is not a

large element of the business in this country. From the very nature of the business it is highly specialized, and a man must devote his life to the trade. The employees are few in a factory, and it is an art rather than a trade.

Senator THOMAS. That being the case, the tax upon pipe organs would not hurt the business much, would it, if the business is practically suspended during the war?

Mr. POUND. Except as to churches.

Senator THOMAS. If a church can at this time afford to buy a \$50,000 or \$100,000 organ, why should it not pay a tax?

Mr. POUND. A great many of these instruments have been contracted for a year ago. It takes two years to make the average large organ. This practically would put a tax not only upon any large purchase but upon matters where bids have been made and where contracts have been drawn, but where there have been no payments made. That is in a large sense the business the pipe-organ people have to-day. If this tax could be left as it is, the words "pianos and pipe organs" being removed and "organ and piano players" substituted, as in the present law, with the exception of the word "organ," which is not there, the business could adapt itself to that condition and could meet it.

Our industry is an industry which is not profiting by the war. We are not at any time what might be known as a profitable business in the sense of big business of to-day.

Senator DILLINGHAM. Before you leave the question of pipe organs, you have referred mostly to the large organs of the large churches?

Mr. POUND. Yes, sir.

Senator DILLINGHAM. Is it not true that the country churches all over the Nation are gradually installing pipe organs—not of the expensive character, but those costing from \$1,500 to \$3,000—and is not that in every instance done by private subscriptions, by the work of the women's societies of the churches, and various similar methods?

Mr. POUND. As to the methods of raising the funds, of course, I can not tell. We do not know.

Senator DILLINGHAM. I ask the question because I placed in the record here a letter from Col. Estey, of the Estey Organ Co., in which he says that the majority of their sales are made under those conditions, after a real struggle on the part of churches to raise the money by subscription, and by holding fairs, and by one thing and another, to get a pipe organ for their churches. I did not know but what you knew something about that from the manufacturer's standpoint.

Mr. POUND. There is no question at all but what the pipe-organ business is perhaps the least profitable business there is in the country. The phonograph is the large and profitable end of our industry.

War conditions have very seriously affected us. We have practically at the present time no men under draft age. They have all gone, and those who have not gone to the Army have gone to munition plants. We are using the women as fast as we can use them, and in the eastern factories a percentage of blind tuners—as much as

80 per cent in some places—so that to-day we are substantially running upon a very curtailed basis. The War Industries Board day before yesterday granted us a supply of metal, under the facts which we are showing to them, sufficient to carry us through upon a curtailed basis of 33½ per cent of our normal production. It is simply a question with us of not attempting to make any profit in this business of ours during the balance of the war, but to preserve sufficient of that organization—the factory and the business organization—to exist.

Senator THOMAS. Why can not concerns which you represent turn out airplanes?

Mr. POUND. We would gladly do it. We can do it better, we can do it quicker, we can do it cheaper than the factories that are doing it. I went to the Government the first week after the opening of the war and tendered every one of our factories. The trouble is that the Government has a hundred factories where it has use for about one.

Senator THOMAS. In that particular?

Mr. POUND. Yes, sir; particularly with woodworking factories.

Senator THOMAS. We heard all over the country during our recent examination that piano manufacturers and manufacturers of other musical instruments have the best facilities for the manufacture of planes, and the query was expressed as to why the Government had not enlisted their services and their organization. I think it ought to be done.

Mr. POUND. It should be done.

Senator THOMAS. We have urged it as hard as we know how, but thus far with no success.

Mr. POUND. Let me give you a concrete illustration. Perhaps the most marked example of housing congestion, of feeding congestion, of street car transportation congestion, of labor trouble, is that at Buffalo, with the great airplane plants there. Before the war started some of our factories were doing the work by subcontract for the Curtiss airplane plant. The moment this cost-plus 10 per cent contract business was installed in the construction of airplanes, the minute these great airplane contracts were given out, our orders were canceled, and great new factories, miles long, were built, creating, as I say, a housing problem, a feeding problem, a rooming problem, a street car problem which has almost ruined the street car system of Buffalo, and every other possible problem. We could have done the work. We begged for the privilege of doing it. But we can not get the work.

I have here a letter to the War Industries Board from the Fuel Administration, saying that they felt that our industry was entitled to some special consideration by reason of the fact that we had tendered our factories for this work. But we were unable to get this work for some reason.

Senator THOMAS. You might add that with regard to the Curtiss factory, with the exception of training planes, they have turned out no planes for the war up to this time.

Mr. POUND. That is true.

Senator SMOOT. There is no incentive to do it as long as they get 10 per cent.

Mr. POUND. Surely the factory that can turn out the Steinway piano or an Estey organ or an Austin organ, or any of these great instruments, can turn out an aeroplane.

Senator TOWNSEND. Do you know whether the Government is paying more now for manufacturing these things than it was paying you?

Mr. POUND. It is more expensive.

Senator THOMAS. You were doing the work for the Curtiss Co., not for the Government?

Mr. POUND. No; not for the Government. We were subcontractors.

The CHAIRMAN. When the Curtiss Co. got these contracts on the cost-plus bases they discharged you?

Mr. POUND. Absolutely and immediately, and they built miles of factories there. Any man familiar with industrial problems knows that you can build four walls, you can put in some machinery, but you can not organize and create a factory in less than a year, or maybe two years. The problem of coordination of labor, the problem of getting the material into and through your factory in an economic, constructive manner can not be worked out in a few weeks or a few months no matter how skilled or how expert the men may be. The result is that those plants, hurriedly built, conceived in hysteria, and built merely in answer to a proposition that they could get these large contracts and could hold them within themselves and not let them get out have disorganized the entire industries of the communities in which they are and have retarded Government work, and usually have done practically nothing.

Senator THOMAS. Do you think if your organization had been given these contracts to assemble these planes they could have put them right side up and right end to?

Mr. POUND. Yes, sir. We have some 20 factories which are doing some Government work—whatever we can get. We are making some munition boxes; we are making some shell cases; we are making some powder containers; we are making some airplanes, some airplane propellers.

Senator THOMAS. Where?

Mr. POUND. The Star piano plant in Indiana, I believe, has a very large airplane contract, and several others of our factories have. Hallett & Davis, of Boston, have airplane contracts.

Senator SMOOT. Granted to them lately?

Mr. POUND. No; some time ago. They are mostly small, subsidiary contracts. I think quite largely they are subcontracts.

Senator LODGE. But in Buffalo they did not use your factory at all?

Mr. POUND. Not one moment, Senator Lodge. After war was declared they immediately notified us they did not need our factory space any longer, and they did need it, because they built miles of new factories there.

The CHAIRMAN. Did the Curtiss people have similar contracts with other concerns?

Mr. POUND. I believe so.

The CHAIRMAN. Did they cancel all their contracts?

Mr. POUND. As I understand it, they canceled everything and built new buildings.

Senator THOMAS. You probably know that the Government provided a great part of the money for the building of those structures?

Mr. POUND. I have understood so. These are the facts. We can not get Government work. We have our factories; we have all our eggs in this basket. We can not get sufficient Government work to live. We are curtailed through lack of material, of course. The War Industries Board has allowed us 33 $\frac{1}{3}$ per cent of our necessary metal. We are not large users of metal, but of course we have to have some. The departments of the Government which are interested in exports have particularly asked us to expend our product as much as possible for purposes of export. The mules of Spain for Pershing's army were paid for by American pianos, and nitrates from South America are coming in likewise. Australia would be a very large buyer of musical instruments to-day if we could manufacture and ship them. The thought that appeals to the various Government bureaus upon the shipping question is that our tonnage of steel is so little in proportion to the selling value of the unit of commodity that it makes a desirable article for export and for the preservation of that trade and gold balance which went behind \$632,000,000 the last fiscal year. I do not mean went on the red-ink side, but went behind the former year.

In shipping we occupy only 80 cubic feet of space, and our instruments are compact in their cases, and make a good shipping proposition, so that every department of the Government to-day is asking us and urging us to produce goods that will go out for export.

Senator LODGE. Do you know anything about the English trade, whether they have not been keeping up their export industry?

Mr. POUND. Yes, Senator Lodge, I can tell you that, and it will be an interesting side light upon the question. The English Government has requested the English piano manufacturers to export, if possible, 60 per cent of their products. We have to-day upon the wharves in New York City 300 pianos, which are purchased for shipment to Australia, and we can not get the British commission here to let us have them go forward. We can to-day supply 85 per cent of the demands of Australia, and of the entire east coast of South America, and the West Indies, and of New Zealand, and of China, which is becoming a good market. We are in a position, if we could be permitted to do business, to supply 85 per cent of that business. But the English manufacturers have, with the sanction of the English Government, formed a corporation of some \$13,000,000. Germany has done identically the same thing. Sweden has, with the exception of the fact that the amount is only \$1,300,000. Those associations are for the express purpose of controlling the export business of the world in musical instruments after the war. It appeals to all governments that the piano proposition largely, the musical instrument industry in its entirety, is peculiarly adapted and beneficial for export purposes, because, as I say, the amount of material entering into it is so comparatively small in proportion to the selling value of the unit that it becomes an export proposition that is favored by all governments. England gives every possible encouragement to the manufacture and export of English pianos.

The CHAIRMAN. Mr. Pound, I understand you to say to the committee that it is the policy of the English Government, with reference to these musical instruments and other like things, not to interfere with or curtail in any way the manufacture of nonessential things for which there is an export market?

Mr. POUND. I do not know that I will make it so strong as that. I mean to say that our reports from the English trade are that the Government very much approves of the export of musical instruments, and makes the request that, if possible, they try and export 60 per cent of their product.

The CHAIRMAN. It is for the purpose, you said, of trying to stabilize and expand their export business in musical instruments?

Mr. POUND. I should believe that would be a fair statement.

The CHAIRMAN. So as to try and control the foreign market?

Mr. POUND. Yes, sir.

The CHAIRMAN. That is a policy with reference to musical instruments. Do you know whether it is a policy with reference to any other articles of exportation?

Mr. POUND. I can not tell you that.

Senator SMOOT. We know, however, that their exports have greatly increased since the breaking out of the war. I do not know of any particular items.

Senator THOMAS. When you say "their" you certainly do not mean Germany?

Senator SMOOT. No, England.

Senator THOMAS. He included Germany.

Senator SMOOT. I meant England.

The CHAIRMAN. The point he was making, as I understood him, was that England did not interfere with the manufacture of non-essential things where those things went largely into the export trade of the empire.

Mr. POUND. I understand they give every encouragement to the export of musical instruments, and I know we get every discouragement here from the British mission in our endeavors to export.

Senator SMOOT. They get every encouragement for nonessential articles of every kind. In fact, England is building up her manufacturing industries, essential as well as nonessential, with all the power she can bring to bear, and it is a wise policy to follow.

The CHAIRMAN. You said a little while ago, Mr. Pound, that you had a large accumulation of instruments ready for exportation to Australia?

Mr. POUND. Yes, sir.

The CHAIRMAN. But that you could not get transportation?

Mr. POUND. The British mission holds us back.

The CHAIRMAN. That means you are dependent upon the British for transportation?

Mr. POUND. No, sir. We have to have their approval of our export license.

The CHAIRMAN. To one of their dependencies?

Mr. POUND. Yes.

The CHAIRMAN. And they decline to give that?

Mr. POUND. They fritter it along a little, but they hold us back.

The CHAIRMAN. Is that on account of any lack of transportation or for the purpose of monopolizing the market in this dependency of theirs?

Mr. POUND. In our belief, it is the latter.

Senator THOMAS. You think, then, there is no problem of ocean tonnage involved?

Mr. POUND. I think there is a problem, but it is getting better every day, and only the other day the Ship Control Board told me they had hoped to give us more space to Uruguay and South America generally. Our pianos are going down there and paying for nitrates and for hide and for beef and for other supplies. And the Department of Foreign Commerce, through Mr. Burwell S. Cutler, director, has been very much interested in the export of our commodities for that purpose. We are told all the time that we will have more shipping facilities, but we do not seem to be able to get them when it is to go to an English dependency. We can send it to Sweden. Only the other day we got permission to send 4,000 actions to Sweden. The German manufacturers are making pianos to-day in large quantities. They lack certain elements in them, and they give an agreement with these pianos which they are sending to northern neutrals—Norway, Sweden, and Denmark—that after the war they will replace any part of the instruments that do not hold up.

Senator THOMAS. Then the condition of Sweden is that, while she has organized a corporation of \$1,300,000 to promote the export trade, she is buying ours?

Mr. POUND. She is buying the internal actions. She has always bought them in Germany, and we were able to get that away. Sweden assembles.

Senator SMOOT. The transports have been taken off between our country and Australia, and England and Australia, in order to carry our troops to France.

Senator THOMAS. That is my understanding.

Senator SMOOT. In fact, I understand that they have been simply robbed of all transportation, and I rather think that is the main reason why you have not gotten your orders to allow the shipment of pianos.

Mr. POUND. It may be. There is a gentleman from Australia in New York to-day. He is representing the retailers of Australia, who have entered into an agreement that for 10 years they will not buy any German-made goods. He has an order for merchandise which includes 900 pianos, among other things. He said last week that he believes he is absolutely unable to get these goods from America, and he is going to Japan. Japan has lately commenced to imitate in our industry the production of our goods, something that she never has done before. While she has been a successful imitator of many American manufactures, she has never been able to produce good musical instruments. Her harmonicas even are very crude. Outside of their own musical instruments, they have been unsuccessful in competing in musical instruments with the rest of the world. They have just made their initial shipment of pianos to South America.

So it seems to me that it is vital to our Government and our organization to encourage preparation for business in the days coming after the war, that we should be permitted to exist and to get along now and to preserve our business and factory organization.

Senator SMOOT. What you want to do is to strike out the words "pianos and pipe organs"?

Mr. POUND. Yes, sir.

Senator SMOOT. And insert "organ and piano players," as the present law provides?

Mr. POUND. Yes, sir.

Senator SMOOT. You do not object to the 10 per cent?

Mr. POUND. No, sir; we believe that we should meet that, and we have organized our business along those lines to do it.

On the floor tax, I direct your attention to the fact that this floor tax is a very radical departure from the present floor tax. That is on page 137, sections 909 and 910.

The CHAIRMAN. I do not take it that you mean to suggest that this Government ought to adopt the policy of permitting manufacture of nonessential articles for export if it would in any way interfere with our ability to get labor and materials for the manufacture of essential war products?

Mr. POUND. Certainly not.

The CHAIRMAN. Your suggestion is that if it can be done without materially interfering with the manufacture of such things as are necessary in these conditions for war purposes, that policy ought to be adopted and that kind of manufacture and trade ought to be encouraged?

Mr. POUND. Yes, sir. And that is the view that has been taken by the War Industries Board, and that question has been decided in our favor by them. The formal order was entered on Saturday.

I might say, in that direction, taking the other view of this matter, that perhaps there is no industry which has profited less from the war and has suffered more from it, and we have done a great work here to help the Government. We gave Mr. McAdoo in the last liberty-loan drive over \$3,000,000, which was 276 per cent over our quota. I venture to give the assertion, strong as it may be, that the liberty-loan drives of this country depended in a very large measure for their success upon the support and the help which our industry gives. We furnish community choruses all over the land; we are sending music everywhere. We are maintaining in my office a bureau which does substantially nothing but send music to the soldiers—free always, of course. We are sending pianos and phonographs and guitars and all kinds of instruments into the camps and into the trenches in France. France has just asked for 2,000 pianos to go "over there," and we are making a small trench piano that can absolutely go into the trenches. There is not a single effort made throughout the country in behalf of these liberty-loan drives and these thrift-stamp drives but what receives the active support of our organization. We are doing our part. This bureau, I will say incidentally, cost us something over \$16,000 this past year to maintain, with a bureau chief at its head, simply to assist in this propaganda and to help along with music these various things.

The CHAIRMAN. Do you suggest that the tax imposed in the House bill is too high? You do not want any tax at all?

Mr. POUND. No; I do not object to the tax at all. We will meet it.

Senator ROBINSON. He wants to strike out the words "pianos and pipe organs" and insert the words "organ player".

The CHAIRMAN. I understood that. You are suggesting, however, that pianos should not be taxed?

Mr. POUND. Yes, sir; pianos or pipe organs, as such, should not be taxed. The pipe organ absolutely can not stand the tax. It would mean an utter discontinuance of the business, and it would be a very serious proposition.

Senator SMOOT. Did you present this to the Ways and Means Committee of the House?

Mr. POUND. Very briefly, Senator.

The CHAIRMAN. Did you present your views before they formulated the bill, and included this tax, or after?

Mr. POUND. Before. But I did not present it as fully at all as I am doing here to-day.

A letter from our President says (reading):

What I fear is an unnecessary curtailment and destruction of the less essential industries, and this may be brought about by the accumulation of material which it is not possible to use as fast as it is received.

And Mr. Wilson said to Mr. McCormick, when he wrote and asked what he should do:

I would far rather have you as a singer for the war than as any other kind of a soldier. We can't all do the same thing. And some one must keep the fountains of sentiment flowing.

Speaking of the floor tax, in section 602 of the old act, which was the floor-tax section, these exemptions were contained. Exempting:

First, a retailer who is not also a wholesaler; and, second, on a manufacturer, producer, or importer thereof.

The manufacturer and the producer and the importer thereof has to pay a tax when he sells the commodity. There is no reason for paying a tax when it stands upon his floor before he sells it. A sales tax is provided for in this new bill, and the sales tax in the act of 1917 especially exempted the manufacturer from the floor tax, because he has to pay the tax when the instrument goes out.

This present bill does not give an exemption for the retailer. I would like to plead his cause. The average piano merchant is an exclusive merchant, from the very nature of his business. He does not carry a supply of groceries or shoes or other commodities. He has a business which is entirely specialized. He has, we will say, a few instruments upon his floor, aggregating possibly \$10,000. A floor tax of 10 per cent upon that man, which must be a cash payment with him, is a very, very serious burden. Those instruments which he has have now paid the present manufacturer's tax. That tax has been paid upon them. He has bought them under that assumption, and to put this floor tax upon him now—and there is no exception in this present tax—imposes a burden on him. In sections 909 and 910 the retailer is not exempt. I say that most particularly in the South and West, where the element of profit in our business seems to be lower than it is in some other parts, it would be a very serious hardship to the merchant, who is not ordinarily a man of large means. It seems to me that sections 909 and 910 should contain the exemptions which are contained in the corresponding sections of the present act.

Senator SMOOT. You would be content with the provisions in section 601 and section 602 of the present law in lieu of sections 909 and 910?

Mr. POUND. Yes, sir; absolutely. Our industry is not, as I have said, a largely profitable industry, and in these war days we are having a terrific struggle to keep our business. It is only by the most careful management and only by going into the highways and byways and getting old men and women and cripples into our factories that we can even keep going. We can not compete with war products in the wages

that are paid, and we can not get war work, except in a very small quantity. It is therefore a problem with us; and this is all we ask of you—to simply let us exist during this war. We do not ask for any large extension of business. We can not get it.

Senator THOMAS. Do you not think that if your organization, as such, your organized capacity, should apply to the Aircraft Production Board—

Mr. POUND. I have done that repeatedly and repeatedly and repeatedly.

Senator THOMAS. As an organization?

Mr. POUND. As an organization.

• Senator THOMAS. That is inexplicable to me.

Mr. POUND. I have gone to every department of this Government trying to get work. In metal-working plants there is plenty of work. But there is not sufficient work for the woodworking plants of the country. As the Hon. P. B. Noyes, the Chief of Fuel Conservation, has pointed out to the War Industries Board, we are an industry which is rather to be favored in times of fuel congestion, because, as a woodworking plant, we use but little fuel. Our waste very largely takes care of our plants. We are not a fuel menace.

The Signal Corps told me a while ago that they had four times as much factory space as they had use for. I said, "Is it not true that you have a hundred times as much factory space offered you as you have use for?" They did not know but what I was right.

There is to-day in woodworking only one shortage of Government needs, and that is handles—ax handles, pick handles, and such things. So far as I can ascertain, that is the only shortage there is, and that is being provided for. They prescribe for that hickory largely, with some ash. There are some concerns in the South which are furnishing hickory, and some can be obtained from the foothills of the Rocky Mountains and in California. But, as a general proposition, there is not enough woodworking for the plants of the country, and such a tax as is provided in section 900 here would be exceedingly disastrous to us. I do not see how we could operate. I do not believe we could, and we are doing our full part in every way, and we are anxious to do it. We will do anything that can be pointed out to us.

The CHAIRMAN. The committee will now hear Mr. S. L. Swarts.

INVENTORIES.

STATEMENT OF MR. S. L. SWARTS, COUNSEL FOR THE NATIONAL DRY GOODS ASSOCIATION.

Mr. SWARTS. Mr. Chairman, I will ask that Mr. Watts, the president of the Third National Bank of St. Louis, who carries a message from the clearing house of the St. Louis banks addressed to this subject, may have a few minutes at the close of my remarks.

We appear in behalf of the National Wholesale Dry Goods Association, an association which includes in its membership practically all of the wholesale houses throughout the United States. We appear here with respect to section 202 of the proposed bill, on page 5, and if I may file at this time and have circulated a brief which I have prepared and which contains these sections and the matters I

propose to advert to from time to time, perhaps it may serve the convenience of the members.

Reading from page 1 of the brief [reading]:

Section 202 of the proposed bill provides:

"~~Sec. 202. Inventories.~~—That whenever in the opinion of the commissioner the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer upon such basis as the commissioner, with the approval of the secretary, may approve or prescribe as most clearly reflecting the income of the taxpayer."

To that section we ask that the following provision be added:

A reasonable allowance being made for the increased cost of merchandise so inventoried over the average cost of like merchandise during the prewar period.

The question that I propose to discuss is one that is not peculiar to dry-goods merchants, but is applicable to every industry in this country whose income is reflected by inventories. The function of an inventory is perfectly clear, and the need of providing for such inventory is the occasion for section 202 in the bill. It is perfectly clear that under normal conditions the use of an inventory is to accurately set forth the income which the business concern has enjoyed during the year. Whether it has made money or has lost money is reflected in its annual inventory. We submit that in abnormal business times, to wit, during the abnormally high prices prevailing to-day, an inventory bottomed on cost in no sense reflects the actual income of a business, and in no sense reflects a profit actually realized or enjoyed by that business in that taxable year.

So that the matter may be clear, reflecting the facts that we are dealing with, I have endeavored, so that the matter may be before you concretely, to take the rise in prices, and you will find them gathered on page 3 of my brief. I am sorry to say the brief was rather hurriedly prepared, and may not be easily followed in some of these things.

You will note, for example, the first group of articles referred to have to do with the dry-goods trade exclusively. You will notice when you turn your eye from the present prices of 1918 and compare them with those of 1915 that there is an average of over 300 per cent difference. In going down the parallel columns, if you will compare 1918 with 1917, you will find that the largest increase has occurred during this present year.

Senator TOWNSEND. Are you talking about retail prices there?

Mr. SWARTS. No, Senator; I am addressing myself to inventory prices. This is the cost to the wholesale merchant.

Senator TOWNSEND. I was out when you started, and I did not get that.

Senator SMOOT. These are all staple articles?

Mr. SWARTS. These are all staple articles.

The CHAIRMAN. You mean the cost he pays to the factory?

Mr. SWARTS. This is the cost at which the wholesale jobber takes his inventory at the close of the year. It is the cost to him. It is what is represented by his invoices from the factory of the manufacturer. So you will notice we have taken hats and caps and gloves. The figures themselves have apparently been the subject of study by Senator Gore, of this committee. I noticed an article by him in this month's Forum, and the prices, as he finds them, are substantially

the prices as we set them out in the schedule. We find he covers some of the same things we do.

An interesting side light on this situation is contained in the comparative cost prices that have been fixed by the Government. It is a price which the Government has established for the manufacturer. These came to me after I had prepared the brief, and there are only eight of these articles that have been fixed, and I should like to state them (reading):

Four-yard 56/60 sheeting: Prewar price, 6½ cents; 1918 Government price, 17½ cents.

Hope 4/4 bleached: Prewar price, 7½ cents; 1918 Government price, 22½ cents.

Pepperell sheeting, 10/4 bleached; Prewar price, 21½ cents; 1918 Government price, 58½ cents.

Six-yard plaids: Prewar price, 4½ cents; 1918 Government price, 15 cents.

Amoskeag staple gingham: Prewar price, 6 cents; 1918 Government price, 19½ cents.

Amoskeag utility dress gingham: Prewar price, 6½ cents; 1918 Government price, 21½ cents.

Nineteen hundred and twenty-one outings: Prewar price, 7½ cents; 1918 Government price, 25½ cents.

Nineteen hundred and twenty-one dark outings: Prewar price, 7½ cents; 1918 Government price, 27½ cents.

The CHAIRMAN. Is that in your brief?

Mr. SWARTS. No. I got these figures too late to incorporate them in my brief.

The CHAIRMAN. Have you more than one copy of that?

Mr. SWARTS. I shall be glad to leave that with you, so that it will go into the record in that shape if that complies with your request.

The CHAIRMAN. Yes; that is all right.

Mr. SWARTS. So that the situation can be before you, and if I may be permitted to show, if you please, assume these few briefs which I hold in my hand represent the amount of merchandise at cost price which the merchant has on hand at the beginning of the year. If you please, he sells that, and he sells it at more than it cost, and he repurchases and again sells at more than it costs, and he repurchases. The result of his operations during the year, if you please, are that he has a stock of merchandise on hand at the end of the year which to-day is in fact no larger in quantity than that which he had on hand at the beginning of the year, but which in aggregate value, at these abnormally high prices, is fully 33½ per cent higher, if not 50 per cent higher, than the cost to him at the beginning of the year.

That is the result of his operations. In other words, a quantity of merchandise that, if you please, represented a cost to him at the beginning of the year of \$6,000,000, at the end of the year, by reason of the sale and repurchase and sale and repurchase, represents to him a cost of \$9,000,000. So that you gentlemen will perceive that what he has really at the end of the year is a profit, if he is compelled to take up this merchandise at cost on paper of \$3,000,000 as a result of these transactions.

It is perfectly clear that the merchant in fact has made no money on these goods that he has on hand at the end of the year, that he can not be said to have made a profit on them until he sells those things, and, so far as his statement for the year is concerned, it certainly can not be maintained that he has made a profit unless and

until he has actually sold those goods at not less than what, under the present regulations, he has been compelled to take up those goods for at the end of the year.

Senator NUGENT. Would he not have made an enormous profit on the goods he had on hand at the beginning of the year and that he sold during the year?

Mr. SWARTS. That is taken up as part of his entire balance sheet. As I suggested, if you please, he had some gingham which he bought at whatever you please, and he sold it at an average of 6 or 7 per cent profit. He has taken the proceeds of that sale and invested it in gingham, but it is constantly increasing in price, and it is perfectly clear that if this merchant can take this inventory at the end of the year, representing \$9,000,000, and it should be proven that that is the same as \$9,000,000 in cash, then he has actually in hand a profit of \$3,000,000. But the difficulty is with respect to treating merchandise which represents a value 300 times over prewar or normal prices as cash in hand. He has undoubtedly made a profit on separate transactions during the year, but that profit is reflected in goods which he has bought and bought again at these increased prices.

Senator THOMAS. In other words, before your supply is exhausted of some particular article, you are going to replenish it?

Mr. SWARTS. We not only have to do that, but we have to have our orders and commitments out so that we may have these things on hand to sell. But I will come to that presently.

Senator SMOOT. Or, in other words, the sales you make are never made at a higher percentage of profit during these times than they are in ordinary times, and when the turnover is made, it is based on what the goods cost at the time of purchase?

Mr. SWARTS. Exactly.

Senator TOWNSEND. Is that a fact? Would you make a larger percentage of profit on the goods you handle than you did before the war?

Mr. SWARTS. That involves two propositions. So far as I have been able to understand the situation, the profit that the wholesale merchant is making to-day is made, first, out of a profit on the selling of the thing which he has at hand and is selling, then an additional profit over what he made in prewar periods, depending on the astuteness of the merchant in having anticipated this increased value of merchandise. In other words, if you had your commitments in six or eight months ahead, then you may have obtained the benefit of a much greater increase in this cost than some competing merchant may have done; in other words, depending upon the astuteness or willingness of the merchants to go ahead and do business in that way. There is where an additional profit has come to him over prewar conditions.

Senator JONES. Do you try to have your commitments equal your sales; or, in other words, do you make arrangements as you are selling these goods to replace them in your stock?

Mr. SWARTS. The answer that I would make to you, Senator Jones, would be this: That business would have to stop if the merchants did not have the distinct commitments out in the hands of factories. As a matter of fact, the factory would come and say, "I wrote you

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1. The first step in the process is to identify the problem or issue that needs to be addressed. This involves gathering information and understanding the context of the problem.

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hand six or eight million dollars' worth of goods on hand at the end of the year, and has commitments out for a like amount of merchandise to be delivered during the course of the succeeding year. He is in the position of having contracts for a total, let us say, of \$20,000,000 of merchandise, with this danger, owing to the fact that that merchandise to-day is three times what it was worth in the prewar period, that a decline, depending on the amount of the decline, is a very dangerous factor with which he has to deal.

Senator JONES. Let me interrogate you a little with reference to your proceeding when you come to the falling market. You say it takes about 11 months to get these goods after you order them. There are no excess supplies in the country at the present time, are there?

Mr. SWARTS. I can not answer that question; I do not know.

Senator JONES. Is not that an important thing for you to know in order to make your point, whether there is an excess supply in the country, and, when the war ends, and whether or not there will be a large quantity of goods dumped on the market at a cheaper price?

Mr. SWARTS. It is my understanding that it is very difficult to get these goods, and that there is not an excess supply.

Senator JONES. That was my idea.

Mr. SWARTS. But I have hesitation in stating that as a fact, because I am not sure of it.

Senator JONES. That is an important fact to be known, and what you have just stated, I believe, is the understanding of all of us. It takes you 11 months to get in new goods. We will assume you are going to get new goods at a reduced price. Will not that give you ample time to sell off these goods, of which there is a limited quantity, at the prevailing price?

Mr. SWARTS. We think not. It has been the past business experience that when a decline comes, it comes practically overnight; that it would be reflected in this way; that all the sales that we have made from merchandise on hand will go through at the new prices and not at the prices at which we held them at all.

Senator JONES. But you make the price, do you not?

Mr. SWARTS. Yes; but the price that is made by the wholesaler to the retailer is not a firm price at all. If there is a decline, the retailer simply takes them at the new price and not at the old one at all.

Senator JONES. How could there be a decline if there is a limited quantity of goods and it will require some months to replenish the supply at a reduced price?

Mr. SWARTS. That may work out in that way. But it seems to me it will take considerable courage.

Senator JONES. Do you not believe that the wholesalers of this country will have that courage and do just that thing after this war is over?

Mr. SWARTS. It would be my best opinion and advice that the wholesalers will not be able to do that thing, and that they will be glad to get rid of their merchandise at the instant of the very first decline, because they feel that a very much heavier decline is coming. They have never yet been able to control that, and it is something that seems to be beyond their control.

Senator JONES. But these times are different from ordinary peace times, and every line of such an industry as you seem to represent

finds it very difficult to replenish its stock, and there will not be any large amount of these goods to dump on the market. The retailers of the country are not stacked up with goods, and why will you not have an outlet for your products at these prices at the conclusion of the war?

Senator SMOOT. May I tell the Senator why?

Mr. SWARTS. Yes.

Senator JONES. I would prefer to have this gentleman answer.

Senator SMOOT. Let the gentleman answer, and then I will tell the Senator why.

Mr. SWARTS. It is the experience of our clients in past years where there has been a situation which has brought about a decline that they have not been able to control it. There was a 20 per cent decline in 1908, in a period of a very short time, and that came very nearly bankrupting a great many of the mercantile houses of this country.

Senator SMOOT. I will say to the Senator also, now, if the gentleman is through, that these goods that are manufactured for delivery are not all manufactured at once; they are manufactured during the 12 months of the year, and they are delivered as they are manufactured; and a merchant that buys them from the manufacturer gets them in about the same proportion as he delivers the goods from his store to the trade.

Senator JONES. I will say to the Senator that I am not wholly without some information on this subject myself, but I wanted to get the statement of the witness in the record.

Senator SMOOT. It is in the record. Now, I have put this much more in the record. And I know that if a merchant can countermand all of his orders it is often done to a manufacturer, and then he has to rely on the goods in his own store, and they will not last very long. If that stock does last very long he is never very much of a merchant, because he has to make a great many turnovers to make any money in these days, during the year.

Senator GERRY. In order to sustain the prices, would you not have to have a very strong combination among the dealers in these goods?

Mr. SWARTS. I do not believe that even that could be done, Senator. I think you would have to have almost a Government regulation or stabilizing of prices to stop what I believe will amount to a panic in this country.

Senator GERRY. In other words, a question of competition comes in there?

Mr. SWARTS. I think so. The situation appeals to them so seriously and the danger to them is so plain, as they see it, that it would take more than an agreement, if such an agreement is lawful, to hold them to a situation of that kind. I do not see how you could control it in any way except by a Government regulation of prices.

Senator GERRY. I was not suggesting that. I was just asking that question to bring out the point.

Senator LODGE. They could not, under the law, make such an agreement.

Senator GERRY. They could not under the law; no. I simply wanted to bring out the point that there was a question of competition there; that was all.

Senator LODGE. Oh, yes.

Senator SMOOT. My experience as a manufacturer has been that whenever there is a marked decline in goods, countermanding the orders is the general rule. I do not care what kind of a contract you have with the buyer, he will find some way or other, either by claiming damaged goods or something, to make up that decline, or else you will simply have to sell your goods to other parties.

Senator LODGE. You mean as a manufacturer?

Senator SMOOT. As a manufacturer. I have had it happen to me a great many times.

Mr. SWARTS. In his speech made in the House with respect to this bill, Mr. Kitchin, on September 5, according to the record, is credited with the saying [reading]:

Have you looked beyond the war to the days of peace, when the reaction that follows every war is sure to come, when the prices of everything are bound to fall one-third and one-half of what they sell for now?

It is my understanding that a decline of merchandise values has followed after every large war.

Senator THOMAS. But not immediately.

Mr. SWARTS. It is very difficult to prophesy whether it is going to be immediate or violent or spread over a period of time.

Senator THOMAS. One can not prophesy; one can draw conclusions from similar events in history.

Mr. SWARTS. It is our feeling that the first definite intimation of peace will bring about an immediate and considerable decline in these values, which to-day represents three times what they were worth in prewar prices.

Senator THOMAS. That will affect the stock market, of course.

Mr. SWARTS. And may I say this, if you will observe, the Government itself has fixed the price of a great many staple articles; that is, has fixed the manufacturer's price. As soon as this war is over, or whenever it may please the Government, it may withdraw those prices, and as soon as those prices made by the manufacturer to us are withdrawn—and those prices are very much larger, as you see, than prewar prices—there will be a shrinkage in values that it is our best opinion is sure to follow, from the fact that the Government has withdrawn those prices. We see no escape from that. We think that is inevitable.

If it be true that a decline is inevitable, let us take a concrete case and see what would happen. If you please, here is a corporation. We will say it has \$5,000,000 capital and \$2,500,000 surplus. That is its condition at the beginning of the taxable year. It has an inventory of merchandise at the beginning of that taxable year, let us say, of \$6,000,000. At the end of the year it has, let us say, an invoice of \$10,000,000, which you will observe represents less, really, in quantity, than the increased cost to it of the merchandise in that year; and let us say that it has commitments outstanding for \$10,000,000 more. Let us say that it has made this year on paper a profit of \$4,000,000 by reason of taking this invoice at \$10,000,000 at the end of the year. That is approximately one and one-half million more—and these are real figures I am giving you—than that corporation made last year, and you see that is at once reflected in this increased cost of merchandise, because I think it is all

related to that and is governed by that. If the merchant must pay, according to the language of this proposed bill, 18 per cent normal tax and 80 per cent war-profits tax, he will pay to the Government, in round figures, \$3,000,000 of the \$4,000,000 his inventory shows him to have made during the year.

And right here let me say that the point that my client is making has no relation to the percentage of the tax at all. We are endeavoring to argue that we should not be taxed until that profit has been realized or is in hand. Now, let us say there is a decline of only 25 per cent within the next six months, or next eight or nine months, in those values. What has happened? This merchant, on his inventory and on his commitments, has suffered a loss of 25 per cent, which is \$5,000,000; he has merchandise of ten million more, and commitments of ten million, and a drop of 25 per cent is a loss of \$5,000,000. What has happened? This \$3,000,000, just like the \$4,000,000 supposed to be profit, is not really cash in hand at the end of the year. This property is represented by merchandise on hand and accounts receivable, and, of course, some cash in bank. It is merged, in other words, with all of his assets.

He has borrowed most of the \$3,000,000 necessary to pay this tax. Six or eight months later there is a decline in values and he loses \$5,000,000. What has happened? His surplus of two and a half million dollars has been wiped out and his capital has been depleted to the extent of 40 per cent.

Senator JONES. I notice the proposed remedy you suggest is to eliminate from the inventory the increase in the value of any asset upon the original cost until such increase is actually realized by sale. Does that meet your difficulty? As I understand it, you have purchased these goods at these increased prices, and if you only want to hold them until you realize the original cost, how does that meet the situation if you expect to sell these goods at cost or at a price below the original cost?

Mr. SWARTS. The remedy which we suggest, I think, is this: We are saying that in taking an account with a man whose income is dependent upon inventory, and whose inventory represents merchandise, if you please, at three times its normal or prewar cost, under rules and regulations prescribed by the commission, a reasonable deduction shall be made from that inventory, having in mind those increased costs. In other words, if I may take an illustration, take the case I put where the merchant has at the end of the year, if you please, an inventory at cost of \$9,000,000. The Commissioner of Internal Revenue, with the assistance of the Board of Tax Reviewers provided for in this bill, as I conceive the purpose of this amendment, would sit in and deal with the facts and figures relating to this particular industry and say that here they have an inventory and we are asking them to pay a tax on an inventory of merchandise that represents three times its normal or prewar prices. We will rule as to that industry, instead of treating this \$9,000,000 as being so much money in hand, or cash in hand, that, if you please, we will treat that as \$8,000,000, and we will allow a deduction of \$1,000,000. And, mind you, that is not a deduction which will enable the merchant to escape the tax, for he has no desire to do that. That allowance runs along and if during the succeeding year the prices are

maintained that tax is absolutely paid to the Government, every penny of it.

Senator SMOOT. That is, the following year?

Mr. SWARTS. Paid at the end of the following year. Then, if at that time prices have either gone up or have decreased again, the commissioner and the board of tax reviewers will regulate this allowance, depending on whether the prices have gone up or have receded, so automatically that will take care of this, to the end that ultimately the taxpayer will have paid a tax only on the profit that he has actually made, and, as we see it and intend it, certainly the Government will not have been deprived of one penny of tax. Nothing, in other words, is tax free.

Senator JONES. Yes; but, as I understand it, the goods have been purchased at these high prices. Is that so?

Mr. SWARTS. Yes, sir.

Senator JONES. If they have been purchased at the high prices, then how would this exemption here give you any relief? You say, "The increase in the value of any asset upon the original cost."

Mr. SWARTS. May I ask from what page you are reading?

Senator JONES. From page 10 of your brief, where you propose to add this to the present law.

Mr. SWARTS. No. The provision I am proposing to add is on the first page of my brief. I have the proposed law and the amendment.

Senator SMOOT. That that section be amended by adding:

A reasonable allowance being made for the increased cost of merchandise so inventoried over the average cost of like merchandise during the prewar period.

Senator JONES. I see. You want to go back to the prewar cost; or, in other words, you want to exempt at the present time the difference between the prewar cost of like articles—

Mr. SWARTS. No, Senator—if you will permit me to interrupt you—I want an allowance as against that, whatever the commissioner's office may consider an allowance on account of that condition. In other words, if I may put it this way, the merchants of this country have for the last two or three years been endeavoring to set aside what they have called reserves, because they have not treated a profit that I insist is largely a paper profit as an actual profit in hand, and so against the inevitable day they have set aside a reserve. That reserve the department has refused to recognize as a deduction.

Senator JONES. How much of a reserve have you set aside?

Mr. SWARTS. As I understand, one concern—I do not know of all of them, but I happen to know about one—set aside two years ago approximately 10 per cent, and attempted to do that last year, too.

Senator JONES. Would you have us leave it to the Treasury officials to fix the amount of the allowance?

Mr. SWARTS. Yes, Senator. I have that proposition to urge here.

Senator JONES. Would you not ask that your business be placed in the same category as other hazardous businesses may be placed in; or, in other words, do you think that in a business of this kind there is an unusual hazard and that some provision should be made for that class of business.

Mr. SWARTS. We think there is a distinct hazard, and that some provision should be made as against that condition and whatever it is—not for us, but for every merchant whose income return is bottomed on an inventory—and that the allowance should be apportioned upon the way in which the prices in that particular industry represent an increase over prewar or normal prices.

Senator SMOOR. Under that plan, if the Commissioner of Internal Revenue allowed a million dollars allowance in the case cited, and during the next year the fall in the cost of the goods did not equal the million dollars, it would immediately show in the next inventory, whatever it may be—\$500,000, \$200,000, \$100,000—or, if the million was represented in the decline, it would show then.

Mr. SWARTS. Precisely.

Senator SMOOR. If that did not show the full million dollars automatically the taxes that would have applied this year upon that allowance—whatever the difference would be—would apply the following year upon the amount?

Mr. SWARTS. Precisely.

Senator THOMAS. May I ask whether under the section as it appears in the bill the commissioner has not the identical power to grant what you want in this amendment?

Mr. SWARTS. I am very glad you asked that question, Senator Thomas. Under the present act there is a broad provision which gives to the Commissioner of Internal Revenue power to enact regulations as may be needed to carry out the provisions of that act. Under that provision it was urged a great many times by a great many merchants that the reserve which they set upon their books against these abnormally high prices, because of what they conceived to be the inevitable day, should be recognized by him as a proper deduction to make before paying the tax. It was recognized that every sane merchant should set up a reserve and should not treat that as a profit. It was recognized by every certified accountant in the country worthy of the name of a certified accountant that it was essential to the merchant to set up a reserve. It was recognized by the Commissioner of Internal Revenue and his experts that the setting up of such a reserve was the proper safeguard, but the commissioner made the point that there was no authority in the bill which permitted him to allow that deduction.

Senator THOMAS. This is not the identical provision.

Mr. SWARTS. No. This, I think, is a very much wider provision. But in order that the commissioner may know that he has the power to do that, we think a specific provision should be put in there. In other words, we do not want that matter to be left in doubt.

Senator THOMAS. You want it absolute instead of discretionary?

Mr. SWARTS. Yes. If the condition is one as we feel exists, if the danger is real, if the situation is one that deserves the consideration we ask, we think it should not be left to the doubtful language in the bill but should be specifically provided for.

The CHAIRMAN. Mr. Swarts, what you are saying would apply to every business in the country equally, would it not?

Mr. SWARTS. It would apply to every business in the country whose return of tax and assessment of tax is bottomed on an inventory and whose business is affected by these abnormally high war prices. Where it was not affected, this condition would not apply.

The CHAIRMAN. It would apply to all business engaged in the purchase and sale of merchandise and other similar products?

Mr. SWARTS. Yes; and probably manufacturers, too.

The CHAIRMAN. So far as corporations are concerned, and so far as the excess-profits tax and the war-profits tax are concerned, if these corporations were permitted to retain a part of their earnings without distributing them, and without them being subject to any tax, they could provide themselves for that condition, could they not?

Mr. SWARTS. I do not see quite how they could do that.

The CHAIRMAN. By not distributing a part of their profits.

Mr. SWARTS. The point that I would make in answer to that is this, that there is no profit until that profit is earned.

The CHAIRMAN. I am speaking about where a profit is earned in a particular year in the case of corporations under the present law. A corporation, under the present law, earns a profit during the year. It ascertains definitely what that profit is, and it distributes a part of its earnings by way of dividends to its stockholders.

Mr. SWARTS. Yes, sir.

The CHAIRMAN. Under the present law it is permitted to retain a part of those earnings for reinvestment in the business, or for any other purpose that they may see fit to do with them in connection with the business. Why does not that afford ample opportunity, if that condition is allowed to exist, and who would not that afford ample protection to the corporation? I am speaking now only of corporations.

Mr. SWARTS. May I answer that in this way, that the corporation, in the first place, is not sure that it has actually made any money at all. After it pays its taxes of \$3,000,000, may I be permitted to say that I do not see where, or out of what, they could set aside any reserve, unless they were permitted to set off an allowance on account of merchandise. They have nothing to set out or safeguard.

The CHAIRMAN. That would probably be true of a corporation that has not made any money at all. But I am speaking of the corporation that has made it. If it has not made any money, it will not have to pay any tax.

Mr. SWARTS. I know I am very dense, but my difficulty is this, that I put a case of a corporation that has made \$4,000,000, and it is a paper profit.

The CHAIRMAN. I understand what you mean. You mean that there are corporations that have made no profits, as a matter of fact, but they have what you call a paper profit, as shown by the inventory that they are required to make.

Mr. SWARTS. The inventory shows a profit, and if those prices are maintained they have unquestionably made that money, and in the ensuing year they have to pay that tax.

The CHAIRMAN. We will go to another phase of it. As I understand you, if you are permitted by the law to build up a reserve for the purpose of protecting you against a contingency of falling prices, that reserve would not be permanently free from the exactions of the Government?

Mr. SWARTS. It is a deduction from the inventory which is not free from taxation by the Government; no, sir.

The CHAIRMAN. It is temporarily relieved from taxation?

Mr. SWARTS. Yes; for that time, unquestionably, and it is reflected again in your inventory during the next year.

The CHAIRMAN. But if in the next year it is made to appear that you have not sustained that anticipated loss by reason of falling prices, then that reserve fund becomes subject to a tax?

Mr. SWARTS. Exactly.

Senator TOWNSEND. Of the year in which it was accumulated?

Mr. SWARTS. Yes, sir.

The CHAIRMAN. Now, with reference to the inventory you have spoken about, have you carefully considered the regulations promulgated by the Treasury Department, No. 33, which prescribes the way in which these inventories shall be taken?

Mr. SWARTS. Regulation 33, affecting the present?

The CHAIRMAN. Yes; the present law.

Mr. SWARTS. I have not that regulation in mind, but I have prepared a great many returns for corporations.

The CHAIRMAN. I am going to read it to you in a minute. Section 202, as I understand, is simply for the purpose of making clear and definite the authority of the Commissioner of Internal Revenue to do what substantially he has done here before by regulation. Here is the regulation [reading]:

For the purpose of returns gross income of mercantile companies shall consist of the total sales plus the inventory at the end of the year less the sum of the cost of goods purchased during the year and the inventory at the beginning of the year.

Mr. SWARTS. Yes, sir.

The CHAIRMAN. As I understand this section is to make definite the authority which promulgated a regulation of that sort. Would that regulation accomplish the purpose you have in mind?

Mr. SWARTS. Oh, no; not at all. We have had this matter up repeatedly for various companies that have been affected by this present tax, and enforcing the present act. You will find that the merchant is compelled to take his inventory at cost, or at value, whichever, if you please, is lower, and as the prices have gone up, of course he has taken them at cost, but never below cost, except, of course, as to a few shopworn things, or things which have lost in value.

The CHAIRMAN. You say this is the total sales made during the year, plus the inventory at the end of the year, and then you subtract, less the sum of the cost of the goods purchased during the year and the inventory at the beginning?

Mr. SWARTS. We feel that the language of section 202 might be construed to give the commissioner the power which we are asking him to exert in the event that he believes an allowance would be proper; but I have seen certain experts connected with the department, and I think, Senator Simmons, that they would say to you that under the language of section 202, as now drawn, they doubt very much whether they would dare to give us this relief if they thought we were entitled to it.

The CHAIRMAN. Did you present this to the Ways and Means Committee?

Mr. SWARTS. No, sir; I was asked to take this matter up just about a week ago.

The CHAIRMAN. Have you conferred with the Treasury Department about this matter?

Mr. SWARTS. I endeavored to meet Mr. Leffingwell, but he was so busy about a matter that he had before the Ways and Means Committee of the House that I was asked to see Dr. Adams, and I saw Dr. Adams for about 35 or 40 minutes. May I state, in view of the question having been asked—otherwise I would not state it—what I understand Dr. Adams's position to be?

The CHAIRMAN. I was going to suggest that there might be some danger of misconstruing his view about it. We are glad to have your view, and we will ourselves ask Dr. Adams and the other authorities of the Treasury Department for their views when we come to that.

Mr. SWARTS. The question was asked whether the commissioner should be vested with such power. May I call attention to sections 22, 212, 214, 217, 222, 228, 234, 252, 603, 1201, 1202, and 1203 of the proposed bill, which, we think, gives as large if not larger discretionary powers to the commissioner; and may I add that the commissioner's office, together with the board of tax reviewers, as contemplated in the present tax, are amply able to, and we feel confident that they will, work out a rule which will be just to the industries of this country whose incomes are affected and just to the Government in such matters? We are perfectly confident that we will get a very fair deal in this matter from that department.

And may I call attention to section 326 of the proposed bill, which deals with invested capital? It is section 326, subsection 3, where the bill provides that there shall not be included as surplus or undivided profits "the increase in the value of any asset above the original cost until such increase is actually realized by sale."

In other words, if a man has either bought or exchanged a piece of real estate during the year, and has on hand a piece of real estate which at the end of the year he might be able to sell at an advance of \$100,000, that \$100,000 is not taxed to him as income because he, in fact, has not realized. And, just so, if there were a depreciation in the real estate he could not claim it as a loss until he had actually sold the real estate and sustained the loss; and we respectfully contend that the provision we are asking for is on all fours with the very language of section 326 of the proposed bill.

Senator SMOOT. That is paragraph 3 of section 326?

The CHAIRMAN. Yes.

Mr. SWARTS. Thank you very much. I think I have exhausted myself and the members of this committee. May I ask that Mr. Watts be given not over five minutes?

The CHAIRMAN. We have been very liberal with you because you have been discussing a very important and interesting question. If Mr. Watts desires to be heard for five minutes—

Mr. SWARTS. I do not think he will take that long. He is here with the Federal Reserve Board Advisory Council attending a meeting.

The CHAIRMAN. We will hear Mr. Watts.

STATEMENT OF MR. F. O. WATTS, PRESIDENT OF THE THIRD NATIONAL BANK, OF ST. LOUIS, MO.

Mr. WATTS. I am president of the Third National Bank of St. Louis, and am representing the St. Louis Clearing House Association.

Mr. Chairman and gentleman, I merely desire to present to you a communication to your honorable committee from my associates in the St. Louis Clearing House Association a document signed by the president of every bank in the city of St. Louis which is a member of the St. Louis Clearing House.

I desire to add that it is a matter of great concern to the banks of St. Louis, and I believe to the banks generally of the country, particularly of those banks that are the purchasers of commercial paper in large quantities. I speak of the bank that I represent, and say that we, among our bills of approximately \$30,000,000, carry from five to ten million dollars of so-called commercial paper—brokers' paper—paper of the larger concerns of the country, having credit upon the general market and not having at hand sufficient banking facilities in the locality in which they are located.

In a situation such as arises out of this question those concerns would be the ones first to feel the injury of the impaired credit that might follow. It has been noticed by the men in charge of the credit affairs of these institutions that during the past two years every statement coming to hand showed a constantly increased amount of merchandise, and a constantly decreasing ratio between the quick assets and the indebtedness of the concern.

Senator TOWNSEND. Do you mean the amount of merchandise or the price of merchandise?

Mr. WATTS. The aggregate of merchandise on hand.

Senator TOWNSEND. In value or in bulk?

Mr. WATTS. In value. There is a point at which danger lurks. In the case of our customers we might look somewhat to the personnel of the customer, we might decide that he would be able to take care of himself in any emergency, and that our obligations from that customer we should carry on; but that is not true of that part of the assets of every one of the larger banks of the country which is composed of the paper purchased on the open market. There it is merely a matter of rule; it is a matter of established principles of credit. It is a well-known fact that there should be a certain ratio of quick assets to liabilities, and that varies with the different lines of business. In the case of the organization which has brought this matter particularly to your attention to-day it has been found from experience that that ratio should be two to one; there should be \$2 of quick assets to each dollar of liabilities; and for that concern to have the best credit in the open market, to have such a credit as the institution that I represent and the other institutions carrying from 20 to 30 per cent of their assets in this class of paper, we will readily purchase the name when offered to us. We find that that ratio has gradually declined in the dry-goods business until we are receiving statements showing 1.85, 1.75, and 1.70.

Senator THOMAS. Is that the only business you notice it in?

Mr. WATTS. No, Senator; I am merely using that as an illustration. The same principles exist with all lines of business where the merchandise has been at a constantly ascending price. We had one of our larger customers, who borrows from ten to twelve million dollars, who has bills outstanding at present of approximately \$11,000,000. come to my office recently and say to me that he hoped that we would not be unduly alarmed if, in his forthcoming statement, his assets showed a ratio of 1.60—a man whose ratio of two years ago was 2.10 to 1.

The question is not whether I am unduly alarmed, the man who carries with his other banker one-third or 50 per cent of his obligations, but the material point is whether those men who buy paper on the open market will be alarmed and will withdraw from him that credit which is absolutely essential for him to carry on the business which he is carrying on at present. That situation, gentlemen, is one which I believe is well worth your deep concern; and it is not a question of taxation, it is not to my mind that the dry-goods man or the shoemen or the hardware men desire to escape any taxation, but it is a question of enabling them to continue their business in such a form that the business of this country will continue to prosper, and they will be able to continue to carry on the business of this country.

I can conceive of no more unfortunate thing in the commerce of this country than to have the credit of the country broken down. It so happens that we are working under, now, a great system of finance, the Federal Reserve System; but it is necessary for them to have fixed standards, and in the banks presenting the paper to the Federal reserve bank for sale to the Federal reserve bank, they are faced with exactly the same principles of credit that our customers, in turn, are faced with when they present their paper to us. Unless the paper is backed by an efficient ratio of quick assets to current liabilities, we find it returned from the Federal reserve bank; and for the business of this country to be put in such a position that those quick assets will decline because of rising inventories and expanding debts to such a point that the Federal reserve banks of the country, that the paper-buying banks of the country, will feel that the credit risk is hazardous, it seems to me that no more unfortunate condition could arise in this country. Gentlemen, I thank you.

Senator TOWNSEND. What is your remedy?

Mr. WATTS. The remedy, Mr. Senator, it seems to me is to have discretionary powers, as has been suggested, so that these concerns may set aside sufficient reserves.

Senator SMOOR. A year ago, when the present law was under consideration, I made the statement that so far as I was personally concerned I would rather compel every corporation in the United States to keep a reserve than to tax every dollar that is earned in order to force it out; and I think if that had been followed, the country would be in a very much better position.

Mr. WATTS. I agree with that position of the Senator, and it seems to me we should rather insist upon the commercial and manufacturing institutions of this country keeping themselves in such a shape that at the end of this war we will be prepared, that our credit will be such that the merchants and manufacturers will be strong enough so that we can instantly rush in whatever the foreign trade is open to us.

Senator TOWNSEND. You agree with the suggestion that has been made by others that if you are exempted from taxation on this reserve at present, and the future should determine that that was not necessary, then the taxation of the deferred years should be imposed upon the exempt?

Mr. WATTS. Yes. Mr. Chairman, I thank you.

(The letters submitted by Mr. Watts are here printed in full, as follows:)

THE ST. LOUIS CLEARING HOUSE,
St. Louis, September 13, 1918.

CHAIRMAN OF SENATE FINANCE COMMITTEE,
Washington, D. C.

DEAR SIR: We, the undersigned, comprising all of the members of the St. Louis Clearing House Association, desire to call to your attention a matter that is, in our opinion, of vital importance to the large commercial institutions, as well as to the banking interests of this country. It is that of making some provision in the new revenue bill that will, in a measure, provide protection against the decline in values of merchandise, etc.

Profits for the current year will be arrived at by inventorying merchandise and factory materials at present prices, which, as is well known, are largely in excess of average values, and beyond question these prices will decline greatly in the event the war should end.

It seems proper and desirable that the law should authorize the setting aside of some equitable percentage of the value of merchandise and materials, or allow a reasonable deduction from the inventory before arriving at the taxable profits, in this way making some provision for depreciation in value which is sure to follow the announcement of the end of the war.

Respectfully,

St. Louis Union Bank, by N. A. McMillan, president; State National Bank, by E. B. Pryor, president; United States Bank of St. Louis, by Otto Peithmann, president; Franklin Bank, by George T. Biddle, president; Central National Bank of St. Louis, by B. T. Edwards, president; Boatmen's Bank, by C. R. Laws, vice president; Mississippi Valley Trust Co., by W. G. Lackey, vice president; International Bank of St. Louis, A. J. Riesmeyer, Jr., president; The National Bank of Commerce in St. Louis, by Jno. G. Lonsdale, president; The Merchants-Laclede National Bank of St. Louis, by W. M. Lee, president; American Trust Co., J. P. Frankford, president; Liberty Bank of St. Louis, J. L. Johnston, president; Mercantile Trust Company, by Festus J. Wade, president; Lafayette South Side Bank, B. G. Brinkman, vice president; Third National Bank, E. O. Watts, president; Mechanics American National Bank, by Walker Hill, president.

The CHAIRMAN. The committee will now hear Mr. McMackin. Please try to be brief, Mr. McMackin.

STATEMENT OF MR. HUGH J. McMACKIN.

MR. McMACKIN. I will do so. Mr. Chairman and gentlemen. I have come here to represent our association, the Eastern Soda Water Bottlers' Association and the American Bottlers' Protective Association and the Virginia Bottlers' Protective Association, who have just held a conference at the Hotel Raleigh this morning, and at that conference it was agreed by all present that we could not ask for any reduction in the proposed 20 per cent tax on our industry, but we felt that there should be amendments made in certain sections of the proposed tax.

We are taxed on nonbeverage alcohol from \$2.20 to \$4.40, an increase of 100 per cent. We do recommend, however, that section 628 be amended, on line 8, page 115, where it reads "a tax equivalent to 20 per cent of the price for which so sold." We are somewhat afraid that the revenue department might construe that to mean that they should levy a tax on our containers. By that we mean on the deposit system that we have on our bottles and cases. Invariably

when we sell our products a great many of the bottlers charge so much for the containers and the goods—so much for the containers and the case—and, of course, when the containers are returned the deposit price paid on the containers is refunded to the customer.

Senator THOMAS. Do you sell the containers with the beverage?

Mr. McMACKIN. Some of the large bottlers do. Most of them do not. And generally when the containers are returned, as is usually the case, the refund is made always to the customer who returns them.

Senator ROBINSON. In those cases you charge the price of the containers against the customer to insure prompt return of the containers?

Mr. McMACKIN. Yes; exactly; the actual cost. We do not make any profit on the containers.

In line 3, in that same paragraph, if the word "so" was stricken out and the words "the beverage is" were inserted, so that it would read "30 per cent of the price for which the beverage is sold," that would obviate any objection.

The CHAIRMAN. You want to make the same change, then, in line 9.

Senator SMOOT. I think you could put it in line 9, and then there would not be any difficulty.

Mr. McMACKIN. Yes; that would be splendid. That per cent clause strikes the near beers, and we are not holding any brief for them. It is the soft-drink industry we are here asking consideration for.

The CHAIRMAN. What would we do about the cases where the seller never intended that the container or bottle should be returned?

Mr. McMACKIN. We would recommend that that should be made to read, "The selling price for which the contents are so sold."

Senator SMOOT. "For which the beverage is so sold"?

Mr. McMACKIN. That would cover it.

Senator SMOOT. But that would not cover the case Senator Simmons speaks of. What are you going to do with a case where you do not expect the container—the bottle, or whatever it is—to be returned—where you do not expect the container ever to be returned?

Mr. McMACKIN. Mr. Martin, of Baltimore, tells me that he ships his beverage to Texas, and the freight charges on the return of the containers are so high that it does not pay him to have them shipped back to him. At the same time, in billing to the customers, they are billed at the actual cost to the factory, the bottles so much and the boxes so much, and there is no profit made on the containers; and we feel, of course, that it would be an injustice to ask us to pay a 20 per cent tax on the container on which we make no profit. On the contents we are perfectly willing to assist the Government, and we want to.

The CHAIRMAN. But where you do not expect the container to be returned, ever, you charge that as a part of the price of the beverage, do you not?

Mr. McMACKIN. The actual cost of that particular item, yes, sir.

The CHAIRMAN. And you want to be relieved from taxation on that container?

Mr. McMACKIN. Yes, sir.

The CHAIRMAN. Do you keep separate accounts of the value of the beverage and the value of the container, where you do not expect the container to be returned?

Mr. McMACKIN. No, sir. They are generally billed out together, and then refunded for on a certain basis. If we allow some bottles—

The CHAIRMAN. I am talking about a case where you do not expect any refund.

Mr. McMACKIN. In Texas we simply bill it out, and, of course, we do not expect them ever to come back, and we figure to lose just the actual cost of what we paid for that merchandise.

Senator SMOOT. You invoice it, then—

Mr. McMACKIN. At the actual cost.

Senator SMOOT (continuing). At the actual cost of the containers?

Mr. McMACKIN. Yes.

Senator TOWNSEND. You charge that cost up to the customer?

Mr. McMACKIN. Yes.

Senator TOWNSEND. You do not lose anything on that?

Mr. McMACKIN. We do not lose anything on it, and at the same time we do not make any profit on it. We bill it at actual cost, and we feel that it should be put so that the department would not expect us to pay a tax on the containers.

Senator TOWNSEND. I can see that very plainly; but suppose you conclude to charge some dealer a profit on the containers which you do not expect to get back?

Mr. McMACKIN. That has never been done, to charge a price on the containers so as to make a profit. We are anxious to get the business on the beverage alone, without making a profit on glass or boxes. It is the beverage end of it; and we believe if your committee will take that into consideration, to change line 8 so that it would read, "the selling price at which the contents are sold," it would eliminate the revenue department from interpreting a tax on the gross sales covering the boxes and the bottles.

The CHAIRMAN. I think this very point has been suggested to us by some other gentleman.

Mr. McMACKIN. It has?

The CHAIRMAN. Yes.

Mr. McMACKIN. Oh, well, then, I will not pursue that further.

There is another question I will take a minute of your time on. On line 12, section b, on the same page, covering natural mineral waters, line 12 reads, "at over 10 cents a gallon, a tax of 2 cents per gallon."

We feel that a great many of the mineral and table water concerns throughout the country to-day are escaping a tax on that industry, and we have recommended that in line 12 it be provided that on all waters selling from 5 to 9 cents or less per gallon, a tax of 1 cent per gallon be levied, and that at or over 10 cents a gallon, 2 cents a gallon be levied, as written in the bill now.

Senator THOMAS. In passing such a tax on, is not the tendency to add something to it and then collect double profits from the consumer, universal?

Mr. McMACKIN. I can say, safely, for the soft-drink industry, that it has not been the policy to do so.

Senator THOMAS. You speak for the wholesalers only?

Mr. McMACKIN. For the wholesalers it has been generally—in our line of industry, it has not been done.

Senator THOMAS. It is very largely the case that the tax has been made the basis for an additional profit.

Senator ROBINSON. The statement was made here this morning by one witness that that practice had prevailed in the soft-drink industry, and he mentioned what he said were specific instances of it, particularly referring to drinks made of soda water; that a tax of 2 cents would just imply an increase in price of 5 cents.

Mr. McMACKIN. At this time, as you gentlemen are probably familiar with, we have been cut down 50 per cent on our sugar allotment, and we expect that the War Industries Board is going to conserve all the lumber, glass, and tin and fuel, and, of course, that will save freight a great deal, and if, Mr. Chairman and gentlemen of the committee, we have permission, we would like to file our brief later in the day, containing the amended suggestions that I have just offered, as we have not had time to submit those, which I have in brief form for the committee's consideration. I would like with your permission to file that later.

The CHAIRMAN. You have that permission.

Mr. McMACKIN. Thank you. That covers all I have a right to say, and I thank you.

The CHAIRMAN. The committee will now take a recess until 3 o'clock this afternoon.

(Thereupon, at 1 o'clock p. m., the committee took a recess until 3 o'clock p. m.)

AFTER RECESS.

The committee reassembled at 3 o'clock p. m., pursuant to recess taken, Senator F. M. Simmons presiding.

Senator TOWNSEND. I would like to have you call at this time, Mr. Chairman, if you will, for a brief statement, a representative of the Burroughs Adding Machine Co. who has asked to be heard on the excess-tax provision, page 129 of the bill—Mr. Dodge.

The CHAIRMAN. How long do you want to be heard?

Mr. DODGE. Not over 15 minutes.

The CHAIRMAN. It is not exactly in the order of our program to call him now, but if there is no objection to that we will hear him first.

STATEMENT OF MR. F. H. DODGE, REPRESENTING THE BURROUGHS ADDING MACHINE CO.

Mr. DODGE. Mr. Chairman and gentlemen, as Senator Townsend says, I appear here to speak for the Burroughs Adding Machine Co., a Michigan corporation, engaged in the manufacture and sale of adding machines, calculating machines, and bookkeeping machines. We are represented throughout all parts of this country and most foreign countries.

My connection with the company is that of director of sales. I am also a director of the company.

What I wish to speak about is the excess section of the new tax bill, page 129, line 8, referring to the 10 per cent tax on adding machines. Until this bill appeared we did not know that it had been proposed to place a tax on adding machines. When we learned this we made some investigation to find out what other countries in the

office-appliance line were covered in this bill. We found some articles had been in the bill which are direct competitors of our products, but those articles had been taken out.

Senator SMOOT. What articles have you reference to as having been taken out?

Mr. DODGE. Typewriters with adding attachments, combination typewriters and adding machines, computing machines, and tabulating machines.

The CHAIRMAN. They have all been taken out, leaving only adding machines?

Mr. DODGE. That is my understanding.

Senator THOMAS. What is a tabulating machine? Is not that a mechanism of somewhat similar usefulness—I mean depending for its patronage upon the same line of trade?

Mr. DODGE. Tabulating machines and duplicating machines; yes, sir. Likewise the combination typewriter and adding machine.

Last Tuesday I appeared before the Ways and Means Committee for the first time, and for the first time stated the position of our company and the belief that we had that an innocent mistake had been made in including adding machines in the form they had been, having later taken out competitive articles.

Senator SMOOT. The mistake was made in dropping the others, was it not?

Mr. DODGE. Well, that is for you gentlemen to judge. After appearing before Judge Hull he asked that I put briefly the main points in a letter, and I think if I read from the letter and then talk from that for a minute or two I can cover the ground in the best way. With your permission I will read this letter, which is dated September 11 [reading]:

BURROUGHS ADDING MACHINE Co.,
Washington, D. C., September 11, 1916.

Judge CORDELL HULL,
Ways and Means Committee,
House of Representatives.

MR. DEAR JUDGE: The war-revenue bill has so far exempted typewriters with adding attachments, combination typewriters and adding machines, computing and tabulating machines, and a proposed tax of 10 per cent is scheduled for adding machines.

About one-half of the product of the Burroughs Adding Machine Co. is known as bookkeeping machines, which come in direct competition with the above classification now exempted.

We believe that the committee are not aware of the fact that this portion of our product is sold for the same use as the three types exempted. We feel certain that there is no intention on their part to show discrimination against any one.

The CHAIRMAN. If we should include those other articles in the bill, would you have any objection?

Mr. DODGE. I beg your pardon.

The CHAIRMAN. I say, if the committee should conclude to include the articles which you say have been eliminated; along with adding machines, would you have any objection?

Mr. DODGE. That would meet the situation partly. My personal opinion is that it might be improved even beyond that. I will touch upon that phase.

The CHAIRMAN. You were basing your argument upon the ground that your machine came in competition with other articles which had been in the bill and which had been taken out.

Mr. DODGE. Yes; that is perfectly true.

The CHAIRMAN. And on the ground that it might affect your business.

Mr. DODGE. Yes.

Senator SMOOT. You are perfectly right on that. Now, come to the tax.

Mr. DODGE (continuing reading):

If adding machines are taxable, then certainly typewriters with adding attachments, combination typewriters and adding machines, and computing and tabulating machines are also taxable, as they are sold for the same purposes as bookkeeping machines.

If the above classification should be exempt, then adding machines should also be exempt.

We herewith place before you certain information showing the essentiality of the adding machine in the business world.

First. About 72 per cent of our product is sold to the Government, war industries, and financial institutions.

Second.—The whole accounting system of the banking institutions is built up around the adding machine. This can readily be ascertained by investigation at Government offices, financial institutions, and manufacturing industries. (Note copies of letters attached.) Forty per cent of our product as represented in money value is purchased by the financial institutions who at present are assuming material responsibilities in handling Liberty loan, Red Cross, War Chest, and Y. M. C. A. accounting for the Government interests, which relieve the Government of considerable expense in this connection. Hence the banking institutions, war industries, Government and Government-controlled institutions would be paying about 72 per cent of the tax. Is it desirable to impose this burden on them, considering that the tax collectible would not compensate for the hardship entailed?

Third.—We estimate that this year's output of Burroughs machines will take the place of 24,000 individuals who would be necessary if adding machines were not in existence. A large proportion of the machines are now operated by women, thereby releasing thousands of men for war work and other duties.

The adding machine is in no sense a luxury. It is a great conservator of man power.

Fourth.—The development of mechanical figuring is so extensive that it requires the services of accountants and highly specialized experts to negotiate the sale with the users, such as banks, railroads, and mercantile institutions, in adapting the machines to their accounting problems.

Fifth.—Many large industries have been so affected by the draft that their accounting departments would be absolutely demoralized without the use of bookkeeping machines. (See letter attached.)

We place the above information before you for your earnest consideration, believing that it is your desire to impose taxation that will be fair and just to all.

Very truly, yours,

F. H. DODGE,

Director of sales; also

Director of Burroughs Adding Machine Co.

If I have your permission, I would like to refer to three short letters, one representing the Federal reserve bank——

Senator THOMAS. Is it your purpose, in referring to these letters, to impress us with the usefulness of this device? If so, I am willing to concede, so far as I am concerned, that it is one of the most useful devices we have to-day in business.

Senator SMOOT. All you have said I can testify to.

Senator ROBINSON. I do not think there is any question about that. Just put in the letters.

Mr. DODGE. I have here three letters, one representing the Federal Reserve Bank System from the Federal Reserve Bank of Cleveland, Ohio. It is not the only letter. Several others are on file with us. There is another letter, representing the national banks of the country, and here is a copy of a letter from the Bethlehem Steel Co. stating how their entire accounting system is built around the machine, and to what extent they are dependent upon it.

Senator ROBINSON. They would be able to pay a reasonable tax, I think.

Mr. DODGE. I think they would, sir. I do not question it for a moment.

Senator THOMAS. They could charge it to cost plus.

Mr. DODGE. I desire, also, to refer to the fact that early in the war our factory at Nottingham, England, was tendered to the British Government for war purposes on the ground that we would be glad to furnish them with such machines as they needed from our American factory. The Government there has had the use of our factory since the beginning of the war. The British Government has conceded or granted our company 20 tons monthly of shipping space to carry machines to Great Britain for use of the British Government, and in the British war industries.

France has already granted 30 tons of shipping space for the same purpose.

So those few developments, coupled with the information you have, coupled with the information about the dependency of the business world on these machines to take care of the labor shortage, I think establish the fact that we do not belong in the classification where we were put when this taxation bill was drafted.

Senator SMOOT. You are classed as a luxury and you are not a luxury?

Mr. DODGE. That point I want to establish beyond any doubt. We are put in the same class as articles such as motion-picture films, tennis rackets, golf clubs, baseball bats, lacrosse sticks, fishing rods and reels, chess and checker boards, chewing gum, candy, dirk knives, bowie knives, daggers, etc., electric fans, thermos bottles, cigar or cigarette holders and pipes, photographs, automatic slot devices, weighing or vending machines, liveries and livery boots and hats, bathing suits, etc.

Senator ROBINSON. Have you taken that matter up with the authorities that make these classifications? You understand that we do not, primarily, make these classifications. We did not assign you to the nonessential or luxury class.

Mr. DODGE. I think my ideas are quite clear on that, Senator, and I think I have established the fact that the article made by our company is in no sense a luxury; that the business world, and financial establishments particularly, are very much dependent on those machines at the present time.

Senator SMOOT. What were you selling the machine at in 1914?

Mr. DODGE. What were we selling it for?

Senator SMOOT. Yes.

Mr. DODGE. With the exception of about one-tenth of our line, the same price as we are selling them at now.

Senator SMOOT. And what is that one-tenth that has increased in price; what line of machines?

Mr. DODGE. Bookkeeping machines, on which we discovered that we made the wrong price in the beginning, when we put the article on the market.

Senator THOMAS. Did you charge too much for them?

Mr. DODGE. We did not charge enough for them, although the raise in price was not very great.

Senator THOMAS. This is not the only type of adding machine? There are other manufacturers?

Mr. DODGE. There are other manufacturers; yes, sir.

Senator SMOOT. This is the machine?

Senator THOMAS. Oh, of course.

Mr. DODGE. I believe our company is providing about 60 per cent of the total number of adding machines used in the country.

Senator ROBINSON. It is a necessary machine in all accounting now.

Senator NUGENT. Are those machines made now which divide and subtract?

Mr. DODGE. Yes; those machines are in this class.

Senator NUGENT. Are machines manufactured that divide and subtract?

Senator THOMAS. They will do everything now except wipe out your overdraft.

Senator NUGENT. I was just wondering whether or not they would be included under this general head of adding machines.

Senator ROBINSON. It ought to be "computing machines."

Mr. DODGE. They are the ones that run in direct competition with the articles that have been taken off the bill.

Senator TOWNSEND. I think there is no question, if Mr. Hull makes that suggestion, that the classification is wrong, and they knew nothing about it at the time, and not until this complaint was made did they get onto it.

Senator JONES of New Mexico. You do not object to the tax you are called on to pay, but to the company you are made to keep; is that it?

Mr. DODGE. I think you will agree that if the Burroughs machine must be sold under a tax while other competing machines and so-called necessities of the business world are sold without a tax, it puts a handicap on the production, not only now but after the war.

Senator ROBINSON. He makes two points—first, that it is a necessity and that it ought not to be taxed in that way; and, second, that if it is taxed other competing articles ought also to be taxed.

Senator TOWNSEND. He puts it right the reverse, as I understand. He does not want to complain about his competitors or anything of that kind, but he wants it put so that if they are exempt he will be exempt. The necessary inference is drawn.

Senator ROBINSON. That is the same, of course. It is a fair proposition, that if he is not exempt and they are exempt it will affect his business.

Senator TOWNSEND. He is not asking you to attack some other item, so far as that is concerned.

Senator ROBINSON. It is a fair proposition.

Senator TOWNSEND. It is a fair proposition.

Mr. DODGE. I suppose every man around this table agrees that it is not fair to leave the discrimination in the bill as it is at present.

I hope you will see that it is fair to exempt adding machines as an essential commodity.

If there is anything else we can add to what I have said, we will be glad to furnish any information. Incidentally, I want you to know that the company has just tendered about 200,000 square feet of floor space to the Government for its use in a most stringent emergency.

Gentlemen, I thank you.

(The letters submitted by Mr. Dodge are here printed in full, as follows:)

FEDERAL RESERVE BANK OF CLEVELAND,
June 12, 1918.

Mr. F. S. CRANE,

Manager Cleveland Agency, Burroughs Adding Machine Co.

DEAR SIR: I am slightly disturbed over your statement that certain minor draft officials have hazarded the conjecture that your repair men are doing non-essential work.

I do not see how the work of this institution could be carried on without the use of adding machines, bookkeeping machines, and other mechanical accounting devices. With the large number of such highly developed and delicately adjusted machines, operated under pressure often by inexperienced persons, and nearly always by persons without mechanical aptitude, it is inevitable that adjustments and repairs should be frequently necessary.

It would seem perfectly apparent that the average mechanic could not be capable of making such adjustments and repairs without the familiarity which results from long training in this highly specialized class of work. Unless we can have at call the service of such experts, the mechanical equipment upon which we have come to rely and without which a tremendously increased number of hands would be required, would be almost absolutely useless, because interruptions to our work would disrupt our entire system, depending as it does so largely upon such dispatch as will insure the handling and forwarding of all items that reach us on the day on which they are received.

These facts are so obvious to anyone acquainted not only with banking but also with the other systems of accounting that are vital to the business interests of the country, that I can not believe that any draft official could be acting with authority in making the statement that your repair men were engaged in unnecessary work. I should think, in fact, that it would be unnecessary to take the matter up with Washington, for it seems inconceivable that such a ruling could be made. However, it is my understanding that the office of the Provost Marshal General (who is, I believe, Maj. Gen. Enoch H. Crowder) would be the proper quarter to which any communications on the subject should be addressed.

Very truly, yours,

E. R. FANCHER, Governor.

BANK OF PITTSBURGH, NATIONAL ASSOCIATION,
Pittsburgh, Pa., July 18, 1918.

Mr. A. W. SAXE,

Manager Burroughs Adding Machine Co., Pittsburgh, Pa.

DEAR MR. SAXE: At this time there is considerable discussion as to "essentials and nonessentials," and from the fact the Bank of Pittsburgh, National Association, operate approximately 40 Burroughs adding machines, it is our desire to issue this letter stating that it would be practically impossible to complete the daily work of any banking institution without the use of adding machines; and further it is a well-known fact that the Burroughs Adding Machine Co. furnish the great majority of adding machines to the different banking institutions in the United States. Should the adding machines be considered as nonessential, it would necessitate the use of at least three times the clerical force in any one of our banking institutions.

Adding machines are so essential to the banking business that we do not hesitate to say that by classing them as nonessential would certainly be a calamity not only to the bank but to the depositor as well.

With kindest regards and best wishes, I am,

Very truly, yours,

WM. M. BELL,
Assistant Cashier.

BETHLEHEM, PA., April 23, 1918.

Mr. F. B. PAULHAMUS,

Senior Civilian Assistant Inspector of Ordnance.

DEAR SIR: With reference to the request and affidavits for the transfer to the Emergency Fleet classification list of Thomas E. Hannahan, of the Burroughs Adding Machine Co., we the undersigned beg to make statement that the Bethlehem Shipbuilding Corporation (Ltd.) is operating 100 per cent on Navy and Emergency Fleet work; the Bethlehem Steel Corporation is operating 65 per cent on Navy and Emergency Fleet work.

All the accounting work made necessary by the operating departments of both these corporations is represented at Bethlehem by a clerical force of 167 on the accounts payable, accounts receivable, and billing departments; 35 out of the total force are constantly at work on the shipbuilding accounts; 86 of the total force are at work on the Navy and Emergency Fleet accounts of the Bethlehem Steel Corporation. Thus a total force of 121 are at work on the accounts made necessary by the Navy and Emergency Fleet work.

This force of clerical workers is absolutely dependent upon the Burroughs adding machines, around which our system of accountancy has been built, and without which it would be almost impossible to obtain the accounting results which are absolutely imperative.

We therefore add this evidence to the affidavits already submitted, with the request that it be given the most serious consideration.

H. G. SMITH,

Manager, Bethlehem Shipbuilding Corporation (Ltd.).

H. E. LEWIS,

Vice President, Bethlehem Steel Corporation.

The CHAIRMAN. The committee will next hear Mr. Wade H. Ellis.

**STATEMENT OF MR. WADE H. ELLIS, REPRESENTING THE
UNITED CIGAR STORES CO.**

Mr. ELLIS. Mr. Chairman and gentlemen of the committee, I represent, as counsel, the United Cigar Stores Co. of America. Mr. Edward Wise, president of the company, had expected to be present, but was unavoidably detained at the last minute, and he has asked me to present his views, which I will do very briefly.

I am not intending to discuss the general tobacco schedule, but only one feature of the tobacco tax, and that is the so-called floor tax, or the tax on goods on hand, which is found in section 702 of the bill, at pages 120 and 121 of your official copy.

Heretofore, under the tax of 1917 and, indeed, under the Spanish-American War tobacco tax, the Congress has always levied on the goods on hand that had already paid the previous tax a so-called floor tax of one-half of the difference between the new law and the existing law; that is to say, one-half of the new tax—the additional burden. This was done in the act of October 3, 1917, passed last fall. There was not the slightest intimation that there was going to be any change in the matter that this time, and it was assumed that the policy would be the same, but the bill as reported to the House provides for the absorption, apparently, of the entire new tax, or the entire difference between the tax imposed by the act of October 3, 1917, and the tax proposed to be imposed by this new statute upon goods on hand; and we respectfully submit that this would be a serious mistake; that the tax ought to be not more than one-half, such as has been the uniform policy of the Government heretofore and such as was provided in the last act.

We ask, therefore, that section 702 be amended so as to introduce the words "one-half of" between the words "of" and "the" in line 5, page 121. of the bill.

Senator SMOOT. The words "one-half of the"?

Mr. ELLIS (reading). "One-half of the difference," etc. This, as I have pointed out, is line 5, page 121.

Now, if the committee please, and will bear with me a few moments, I would like to read very briefly, and I will save the time of the committee in that way, the several distinct reasons given by the president of the United Cigar Stores Co. for this proposed amendment. In order to make this clear I will read Mr. Wise's statement in full [reading]:

STATEMENT OF EDWARD WISE, PRESIDENT OF UNITED CIGAR STORES CO. OF AMERICA.

(Title VII, sec. 702, H. R. 12863—Floor tax on cigars, tobacco, and manufactures thereof.)

We respectfully ask the amendment of Title VII, section 702, H. R. 12863, by inserting, on page 121, line 5, between the words "to" and "the," the words "one-half of," so that section 702 shall read as follows:

"That upon all the articles enumerated in sections seven hundred or seven hundred and one which were manufactured or imported and removed from factory or customhouse on or prior to the date of the passage of this act, and upon which the tax imposed by existing law has been paid, and which are, on the day after the passage of this act, held by any person and intended for sale, there shall be levied, assessed, collected, and paid a floor tax equal to one-half of the difference between (a) the tax imposed by this act upon such articles according to the class in which they are placed by this title, and (b) the tax imposed upon such articles by existing law other than section four hundred and three of the revenue act of nineteen hundred and seventeen."

The existing revenue law, being the act approved October 3, 1917, in section 403 thereof, provided as follows:

"That there shall also be levied and collected, upon all manufactured tobacco and snuff in excess of one hundred pounds or upon cigars or cigarettes in excess of one thousand which were manufactured or imported and removed from factory or customhouse prior to the passage of this act, bearing tax-paid stamps affixed to such articles for the payment of the taxes thereon, and which are, on the day after this act is passed, held and intended for sale by any person, corporation, partnership, or association, and upon all manufactured tobacco, snuff, cigars, or cigarettes, removed from factory or customhouse after the passage of this act but prior to the time when the tax imposed by section four hundred or section four hundred and one upon such articles takes effect, an additional tax equal to one-half the tax imposed by such sections upon such articles."

The act of October 3, 1917, so far as concerned the war tax on "Tobacco, cigars, and manufactures thereof," did not become effective upon its passage, but became effective 30 days after the passage thereof, and it was for that reason that the provisions of section 403 were extended to tobaccos, etc., removed from the factory after the passage of the act but prior to the time when the tobacco tax became effective. The new House bill makes the changes in the rates of taxes on cigars, tobacco, and manufactures thereof effective at once. It is not asked now that there be any extension of time of 30 days or otherwise before the floor taxes on goods on hand at the time of the passage of the act become effective, but it is asked that the floor tax should attach immediately on the day after the passage of the act, as provided in section 702, upon all goods then held and intended for sale. It is, however, respectfully submitted that the amount of this floor tax should not represent, as now provided in section 702, the whole of the difference between the tax imposed by the new law and the tax imposed by the existing law, but should, for the following reasons, equal only one-half of that difference.

I.

In order to collect this floor tax it is necessary that an inventory be made by every jobber and retailer of tobacco and manufactures thereof. Under a previous revenue act, by which an occupation tax was imposed upon all jobbers and retailers of tobacco products, there were registered in the whole country 485,000 of all kinds, small and large. Statistics which are believed to be

reliable, obtained through the Treasury Department, show that the returns on the floor tax imposed by section 403 of the act of 1917 were made by only 10,000, and that the total amount of the floor tax so collected was \$5,191,724.84. It is conservatively estimated that at the time of the passage of the act of 1917 there were in the United States not less than 600,000 dealers in tobaccos and manufacturers thereof at retail; this did not include jobbers.

At the time of the dissolution of the American Tobacco Co. in 1911, under the decree of the United States Supreme Court, the record in that case showed that there were at that time over 600,000 persons and firms engaged in the United States in selling tobaccos and manufactures thereof at retail, and yet in 1917 returns for the payment of the floor tax were made by only 10,000. The collection of the floor tax from the retailers under all circumstances is difficult, and to collect even a portion thereof requires a staff of thousands of men. The result has been that practically only the largest among the retailers and jobbers filed returns as required by the regulations and paid the amount of the floor tax, and this was on the basis of the payment of one-half only of the additional tax.

II.

The stocks of tobacco and manufactures thereof which the dealers will have on hand on the date of the passage of the new act will all represent purchases made by the retailers long prior thereto, due in large measure to the fact that the Government requirements for the Army and Navy have been so comprehensive that the retailers have been obliged at times to wait for months beyond the ordinary time in order to receive goods ordered by them, all realizing that the Government requirements must first be satisfied. These goods have all been purchased on the basis of the present revenue acts. Increased taxes in the act about to be passed will require increases in prices in tobacco and the manufactures thereof by the retailers to consumers. It is, of course, the retailer, and not the manufacturer, who comes in contact with the purchasing public. The retail prices can not be so readjusted as to be changed overnight.

III.

The retailers are satisfied that with regard to all goods purchased either before or after the passage of the new act, and which are not held by them one day after the passage of the act, the full tax imposed by the new law should become effective the day after the passage of the act. A different situation, however, exists with regard to stocks on hand which are large, due, as above noted, to the necessity of retailers getting goods when they could and carrying them in as large quantities as their capacity and credit will permit. As to these stocks on hand and which in the case of large retailers are turned over in about 45 days, the changed sizes of the packages, the changed sizes of the cigars, and the general readjustment necessarily involved by the largely increased taxes will render it practically impossible for retailers to readjust their prices to the consumer within a period of less than 30 days after the passage of the act without entailing great loss, which there is no possibility to recoup, upon the part of those retailers who will comply with the law and make the returns and pay the tax pursuant to the rules and regulations of the Commissioner of Internal Revenue.

IV.

The amount of the floor tax paid by the United Cigar Stores Co. of America pursuant to the provisions of section 403 of the act of 1917 was \$233,117.26. The time and the efforts of all the officers and employees of the company were immediately directed to readjustment of the business so as to meet conditions imposed by the change in the tax. Notwithstanding all efforts made in this regard it was found to be entirely impracticable to make adequate readjustments involving increases of prices for a period ranging from one month to three months after the passage of the act. Increased prices on cigarettes and tobaccos to the consumer to meet the requirements of the new taxation did not become completely effective until December, 1917; on cigars the readjustment was not made until about 90 days after the passage of the act, due to the fact that the manufacturers were unable to make new sizes to meet the new conditions, and in the meantime the old retail prices prevailed on stock on hand. There were a few exceptions on a few publicly advertised brands, but not material enough to affect the general result.

V.

Under the Spanish-American War act, increasing the internal-revenue taxes on tobacco products, it was provided that stock on hand should pay one-half of the new tax under the same conditions as the act of 1917. It was estimated that there were 400,000 retailers in the United States in 1898, and of this number there were only 4,329 who made returns. There were 34,000 manufacturers and only 345 made returns. The total amount of the tax collected was \$919,000.

VI.

For the foregoing reasons, and in order that undue hardship may not be placed upon those retailers who have always complied with the law and who will comply with the new law, as against the larger number who have failed to make returns and in that way have failed to pay the tax to the Government as required by law, it is respectfully submitted that the interests of not only these retailers but of the Government itself will best be served by imposing instead of the whole tax an amount equal to one-half of the tax only as such floor tax, and at the same time through the Internal Revenue Department to arrange, so far as possible, for a complete enforcement of the law.

VII.

The position which I have outlined as representing my company is not peculiar to my company. It is the position of every retailer in the country who is anxious to comply with the provisions of law to enable and to assist in every way in raising as large an amount of revenue as possible out of our own industry without unnecessary destruction. I am informed that a brief has been filed or is about to be filed with this committee by the Tobacco Merchants Association of America, which represents among its membership thousands of jobbers and retailers throughout the United States who are in no way affiliated with the company which I represent, and who are earnest competitors thereof, and I invite the attention of the committee to the consideration of the views expressed by that association in its brief.

September 16, 1918.

Respectfully submitted.

EDWARD WISE, *President.*

The FINANCE COMMITTEE, U. S. SENATE.

Mr. ELLIS. Now, Mr. Chairman and gentlemen, I have no reasonable doubt that if these facts had been called seasonably to the attention of the Ways and Means Committee the correction we suggest would have been made by that committee.

Senator THOMAS. It would appear from your statement that previous and existing laws are manifestly weak in the machinery they provide.

Mr. ELLIS. I should say, perhaps, in the enforcement.

Senator ROBINSON. Did you say that out of 600,000 who were liable for the tax only 10,000 made returns?

Mr. ELLIS. Yes, sir.

Senator SMOOT. There was 10 per cent paid the tax, but far less than 10 per cent of returns—

Senator ROBINSON. I understood you to say that there were only 10,000 out of 600,000 that were liable for the tax.

Mr. ELLIS. Yes.

Senator THOMAS. With that law in force as it ought to be, the revenue from tobacco would be very much greater.

Mr. ELLIS. Yes, sir.

Senator THOMAS. Could you tell us how much the estimated revenue from this source would be reduced by making the amendment you have suggested? Have you figures on that?

Mr. ELLIS. I do not know the Treasury Department's estimate, but I do not believe it would be reduced at all by the change we propose.

Senator ROBINSON. He can not tell, but they have estimated a given amount of revenue to be derivable from this source, and of course if that estimate is reliable, we could get the amount to be derived under the bill as amended by simply dividing it by two.

Mr. ELLIS. But it must be remembered that while one-half the additional tax on floor stock might be absorbed by the seller before the readjustment of prices or sizes, the entire additional tax could not be so absorbed; and if experience shows that a vast majority of dealers made no return of stock on hand, in order to evade one-half the added tax, it would be still more difficult to collect from all if the trade were subjected to the entire increase in taxes, with no opportunity of recoupment. All things considered, it would seem fairer to impose a floor tax which all can pay and then strictly enforce it as to all.

Senator TOWNSEND. I want to corroborate what Mr. Ellis has said by facts that have come to my attention. I am not acquainted with anybody connected with the United Cigar Stores except Mr. Ellis, and I did not know that he was so connected until I saw him stand up here, but we have these stores in innumerable towns in my State. Immediately after we passed the act of October 3, 1917, practically every one of the smaller stores raised the price of certain tobacco about 20 per cent on certain qualities of tobacco that I have in mind. The United Cigar Stores did not do that, and they had not raised it when I came away last, four weeks ago. It was still at the same old prices they had always charged, for the last 4 years, and on a 5-cent package of tobacco the others were charging 7 cents. The United Cigar Stores were selling it still at 5 cents. They had paid the tax, and neither of the other stores I have in mind, I am positive, had ever paid a cent.

Mr. ELLIS. Probably they have made no returns.

Senator TOWNSEND. No.

Senator SMOOT. Does the Internal Revenue Department intend that 98½ per cent of the tobacco dealers of this country shall escape paying taxes on their floor stock?

Mr. ELLIS. Of course not, Senator; the Internal Revenue Department means faithfully to perform its duty.

Senator ROBINSON. Do you know whether or not that statement has ever been called to the attention of the Commissioner of Internal Revenue?

Mr. ELLIS. I do not know, Senator.

Senator SMOOT. It is so astounding that I can hardly believe it.

The CHAIRMAN. Is not this true: Does not that 600,000 include every little dealer that had a box or two of cigars upon their floor when the tax went into effect?

Mr. ELLIS. I think that is quite likely. It must include a number of dealers that it would hardly pay to get the tax from.

The CHAIRMAN. Under the present law we allowed 30 days after the passage of the bill before it went into effect.

Mr. ELLIS. Yes, sir.

The CHAIRMAN. Then, in addition to that, under the present law we allowed certain exemptions.

Senator SMOOT. One hundred pounds of tobacco and 1,000 cigars.

Mr. ELLIS. Yes.

The CHAIRMAN. One hundred pounds of tobacco and a thousand cigars.

Mr. ELLIS. Yes.

Senator ROBINSON. That would unquestionably eliminate a great many of them.

The CHAIRMAN. Yes. It would not account for all of them. But the small dealers all over the country, who had a small stock on hand, they are included in that 600,000, and they disposed of their stock in some way or other before the end of that 30 days—many of them; many of them disposed of the stock that would not be exempt under the tax.

Mr. ELLIS. Doubtless that is so.

The CHAIRMAN. I have the number of dealers in the United States stated here as 477,766. Out of that number he says only 10,000 made returns.

Senator SMOOT. The difference between the number of those who made returns and the total number of dealers is appalling.

The CHAIRMAN. Yes; but you know every little country store and little stores selling other things everywhere will carry a few cigars, incidentally—a very small stock.

Senator SMOOT. One hundred pounds is a good deal of exemption.

Senator TOWNSEND. All those little fellows took advantage of it and put up the price.

Senator ROBINSON. I understand that the Commissioner of Internal Revenue is not asleep on the proposition, because he is a very active man. He gets the revenue.

The CHAIRMAN. The committee will next hear from Mr. George A. Lee.

STATEMENT OF MR. GEORGE A. LEE.

Mr. LEE. Senator Lodge and gentlemen of the committee. I can say what I have to say, I think, in less than 10 minutes.

I regret that I did not have the opportunity of hearing what the oil men had to say two or three days ago upon the depletion clause of the revenue bill. Accredited representatives of the German Government have stated within the last 60 days that when the belligerent nations now engaged in this contest sit around the peace table to discuss the terms of peace, the potash of Germany will have a large part to play in dictating what those terms of peace shall be.

Senator ROBINSON. Maybe so.

Senator THOMAS. Maybe so.

Mr. LEE. That threat has been conveyed generally throughout the world, and has reached this country, and was intended to reach this country.

For the information of this committee I want to say that the State of Nebraska, probably much to your astonishment and much to the astonishment of everyone two or three years ago, is now producing from 60 to 80 per cent of the potash supply of America.

In 1913 the German Government imported into this country under the syndicate plan, which now prevails there in the production of their potash, some 287,000 tons of potash—287,000 tons which was cut off entirely at the time war was declared.

Last year Nebraska, in cooperation and conjunction with other potash producers in this country, was able to produce but 32,000 tons of potash. This year that production will probably be doubled, because the potash plants of Nebraska—

Senator LODGE. What was the tonnage they produced?

Mr. LEE. Thirty-two thousand tons was produced by the American industry last year, as against an importation of some 250,000 tons the year before war was declared.

Senator SMOOT. We produce more potash than that. Nebraska may have produced 32,000 tons, but more was produced in this country?

Mr. LEE. Yes, sir; others produced that.

Senator SMOOT. You said "we."

Mr. LEE. That was a mistake on my part. Nebraska produced from 40 to 50 per cent of the production of this country.

Senator SMOOT. Utah produced nearly 20,000 tons last year of potash.

Mr. LEE. I am speaking from my only available data—the reports of the Geological Survey and the reports to me from the Department of the Interior and the Department of Agriculture.

Nebraska potash, as well as potash from all other parts of the country, is used largely and fundamentally in the South and East, essentially for fertilizer purposes.

Senator THOMAS. It is also very valuable in mining, for the separation of gold.

Mr. LEE. Yes. The bulk of it at this time is going south. I can say all that I want to say on that by one or two concrete examples.

The CHAIRMAN. What is the prospect of expanding that production?

Mr. LEE. The prospect of expanding it depends upon the prospect of the new revenue bill and the consideration which Congress is disposed to give to such war mineral industries as the potash industry. I can just answer your question by taking one concrete case.

The CHAIRMAN. Suppose we eliminate that and say that everything is done that is necessary to be done to stimulate the industry.

Mr. LEE. That is very favorable, I am sure.

The CHAIRMAN. To what extent can you expand it?

Mr. LEE. We can expand it to the absolute exclusion and perpetual exclusion of German potash.

Senator THOMAS. How long do you think it would be before you would produce an adequate supply?

Mr. LEE. I would say that with the present production continuing as it is now, under reasonable protection, and permitting the capital investment to be amortized, within three to five years the production should equal if not exceed the German importations.

Senator SMOOT. In order to do that, however, the producer in this country has got to be assured that after the war he will have the American market?

Mr. LEE. Oh, exactly.

Senator SMOOT. In Utah to-day we have absolute mountains that we can produce potash out of, all you will want in the United States for the next 100 years; but the price, of course, of producing it and the freight rate to the market is so much higher than it is in Germany that it can not be done.

The CHAIRMAN. Is the production very costly?

Mr. LEE. Quite costly, as compared with the German production. Over there they mine it and here we manufacture it.

Senator SMOOT. Are the lakes in Nebraska going to hold out long?

Mr. LEE. It has been estimated by competent geologists that under the present degree of depletion they will probably last from 10 to 15 years.

Senator THOMAS. At what rate of production?

Mr. LEE. That is at the rate of production in the coming year, which will be about——

Senator SMOOT. Sixty thousand tons?

Mr. LEE. Yes; about 60,000 tons. There is a potash plant being completed now, which was started some months ago, at Antioch, Nebr., which cost \$1,250,000.

The CHAIRMAN. What is the capacity of that plant?

Mr. LEE. It has a capacity of about 800 tons of potash per day. The brine lakes which adjoin this plant are ample and sufficient to supply the plant for years to come. Under the present law, and the revenue bill as crystalized into law last year, that plant will have to pay between \$200,000 and \$250,000 to the Government. They see no assurances of amortizing their investment. If this war suddenly concludes, no one can forecast the future. No one at this time, of course, can predict congressional action—congressional action with reference to the exclusion of German products.

We all hope that an American policy will be pursued regardless of politics, but that is a contingency of the future, and the situation which now must be met by that company and other companies similarly located, representing an investment of between eighteen and twenty million dollars in Nebraska, is this, are they going to recover their capital investment out of their returns, if they are to be taxed between 60 and 80 per cent under the present law? The Treasury Department is helpless. They have told my company and other companies that they ought to get relief, and in order to stabilize and in order to put this American industry on a solid foundation we would very much like to see it accomplished; and after conference with Chairman Kitchin and the Ways and Means Committee, a depletion clause was written into the bill which is now before this committee for consideration.

Senator THOMAS. What Treasury Department official gave you that assurance?

Mr. LEE. Dr. Allen. I understand, mining expert of the Treasury Department.

Senator THOMAS. Did he convey it to the Ways and Means Committee?

Mr. LEE. Yes; Dr. Allen told me——

Senator THOMAS. Is it your contention that the Ways and Means Committee disregarded it?

Mr. LEE. No, Senator; my contention is that the bill as it now stands will give reasonable relief.

Senator ROBINSON. Oh, you are satisfied, then, with the relief you have in the bill as it is?

Mr. LEE. Yes; and I simply wanted to take a few minutes of the time of this committee to point out the importance of it.

The depletion clause as it now stands in this bill involves the human equation, and that, of course, is necessary in the administration of this bill or any other bill, but we are willing to take a chance on this committee. While Dr. Allen does not represent directly the Internal Revenue Commissioner, I am willing to take a chance on the integrity of such representations. He told me that this language was intended to accomplish the amortization of the capital investment. I do not see how that position can be successfully assailed. If a man is willing now to undertake the investment of a million or a million and a half dollars in order to stabilize and build up some industry, it seems to me that he ought to be permitted to at least set aside a portion of his net profits to take care of his capital investment before he is taxed from 60 to 80 per cent.

These potash plants, Mr. Chairman and gentlemen of the committee, are not seeking entire immunity. They are not seeking to have their capital investment written off with one stroke of the pen. They are as patriotic as any other class of citizens. They are willing to do their bit, and they are doing it; but they do feel that if the earnings of a certain year, for instance, are \$300,000, \$100,000 of the \$300,000, under reasonable rules and regulations of the Treasury Department, should be set aside out of their net earnings to permit them to help amortize the \$1,250,000 investment. Or, if the war suddenly concludes, and it is seen that foreign potash may enter this country to the exclusion of domestic potash, then they feel that the spread ought not to be so limited but that they ought to get a greater part of their net earnings of that particular year to take care of their capital investment.

Senator JONES of New Mexico. You have remarked that the rate of taxation on your industry will be 60 to 80 per cent.

Mr. LEE. Yes, sir.

Senator JONES of New Mexico. How do you figure that out?

Mr. LEE. Only by the returns which are estimated by the Internal Revenue Commissioner and the money which has been paid.

Senator JONES of New Mexico. Then your rate of profit is very high, is it not?

Mr. LEE. Yes; the rate of profit has been very high, Senator, and that is the very proposition that has stimulated the investment. There is no question but what the profit in potash is extremely high at this time.

Senator JONES of New Mexico. How much are you getting from your potash now?

Mr. LEE. I can not speak from the operating end of it. I only represent them in a legal capacity, on legal questions and rate questions.

Senator THOMAS. Can you not give us some idea?

Mr. LEE. I think that the Nebraska and other production in this country is selling for from five to ten times what German potash brought before the war.

Senator JONES of New Mexico. That was my recollection.

Mr. LEE. And, of course, the cost of production is infinitely greater.

Senator THOMAS. But not five or ten times greater?

Mr. LEE. Yes; but, Senator, if a man is willing to risk a million or two million dollars—

Senator THOMAS. I am not finding fault. I am from a mining country and know what the hazards of the business are.

Mr. LEE. I know that you are, and that is why I was going to say if a man is willing to put up a million dollars or two million dollars at the solicitation of the department he ought to be assured of the protection of his capital. Take this \$2,000,000 plant that is being built and will be operated in southern Nebraska; it does not own a lake, but it leases all the potash lakes around it upon a royalty basis of 20 per cent. Under the present bill it is not permitted a nickel for the depletion of those lakes, and yet any intelligent man would immediately conclude that just to the extent that those lakes are depleted—25, 50, or 100 per cent—just to that extent is the value of this potash factory impaired and destroyed.

Senator TOWNSEND. You mean under the present law?

Mr. LEE. Under the present law. Now, I take it that the Treasury Department, without having given the matter very careful attention, have arrived at this expression, which seems to be fair, that there shall be an equitable apportionment between lessor and lessee, which, as I construe it, would mean that if that string of potash lakes which supplies this factory is depleted 50 per cent, for instance, during the next year, then the allowance which is made for depletion will be set aside and will be equitably proportioned between the lessor—who has not a nickel in the lakes other than what it may have cost him years ago—on the one hand, and the factory on the other.

The CHAIRMAN. You are satisfied with the bill in this respect as reported?

Mr. LEE. Yes, sir; satisfied with the wording of it.

The CHAIRMAN. You simply want to impress it upon us?

Mr. LEE. I want you to appreciate the importance of it.

The CHAIRMAN. Just one question. Have you stated how long, in your judgment, these potash lakes would furnish an adequate supply?

Mr. LEE. The best available opinion is from 5 to 15 years. My own judgment, having seen them and having seen the potash deposits in them, is 15 to 20 years; but the State geologist of Nebraska tells me 15 years.

The CHAIRMAN. You think, then, in 15 years our available supply in this country will be exhausted?

Mr. LEE. So far as the brine lakes of Nebraska are concerned. I understand, however, that experiments are being attempted by the Department of Agriculture to extract potash from some other minerals.

Senator THOMAS. Yes. Great Britain is manufacturing a large part of her potash from other materials.

Senator LODGE. There are great deposits in Utah also.

Mr. LEE. Yes.

Senator LODGE. Also in California and the Searles Lake region.

Mr. LEE. Yes.

Senator THOMAS. The deposits in our country do not, I think, exist in the form of lakes; they are in rocks, more.

Senator ROBINSON. What is the output of Searles Lake now?

Mr. LEE. I have not been advised.

Senator JONES of New Mexico. You have a big plant there.

The CHAIRMAN. What you mean to say is that the present law would supply this country for 15 years, but you have no information

as to how long the total potash supply of the lakes in the country would be equal to our demand?

Mr. LEE. I have not, Senator; but knowing what I do about the experiments that are being conducted and the results that are being obtained, I am very sanguine about the future.

Senator THOMAS. No doubt about it.

Mr. LEE. I think if you will take this letter which was placed before the Ways and Means Committee, which came to my attention two weeks after it was received by the committee—it is a very succinct representation of the attitude of all of the people of the country—that unless they are permitted to amortize their investment the industry will not expand. I thank you for your attention.

The CHAIRMAN. Mr. L. C. Boyle desires to be heard, and we will give him the opportunity now.

STATEMENT OF MR. L. C. BOYLE, COUNSEL FOR THE NATIONAL LUMBER MANUFACTURERS' ASSOCIATION.

Mr. BOYLE. I would like to call the attention of the committee to line 24 on page 38 of the House bill, which comes under section 234, under the head of "Deductions allowed," under the income-tax provision.

The thought that I am seeking to convey was not discussed before the House committee, and, as a result, I am of the opinion that the matter that I have in mind was omitted from this bill, and I think all that will be necessary will be to call your attention to the omission [reading from the bill]:

In the case of oil and gas wells a reasonable allowance for actual reduction in flow and production to be ascertained not by the flush flow but by the settled production or regular flow; (b) In the case of mines a reasonable allowance for depletion; (c) in the case of mines, oil, and gas wells, a reasonable allowance for depreciation of improvements.

That language under (c) is the principal thing I wanted to call your attention to.

Now, my point is that there is no reason in the world for making that provision to include oil and gas wells and not as to a lumber manufacturing business, because the parallel between the production of a coal mine, for instance, which is a destructive industry, and the depletion of a timber block which is operated by a sawmill, is perfect. They are identical.

Senator LODGE. Trees, however, grow again, and coal does not.

Mr. BOYLE. I will speak of that, Senator.

Here is a practical proposition, and those of you who come from lumber sections will appreciate my thought, that a sawmill is built only after the timber to supply it is bought. That is not altogether true upon the west coast, where they have mills that buy their logs for their daily consumption, but in the South and in the Lake region and in the Atlantic coast region and in all other sections of the country, excepting upon the west coast, the timber is bought and then the mill is built. Now, for a modern mill, equipped as they must be now to operate effectively, it is necessary to buy a tract of timber for 15 or 20 year operations. A 15-year operation is considered, by those who have given the matter scientific study from an industrial

and economic standpoint, to be the mean average of what would be necessary.

Now, to Senator Lodge's thought. It is impossible, of course, for the operation of a sawmill that has got a 15-year cut, to rely upon any reproduction process of the trees during the actual life of that mill.

Here is my idea, and I think this is so manifest, gentlemen, that when you come to put your minds to it you will see that I must be right. A coal mine is developed. It has an acreage of coal to be exhausted. A shaft is sunk at a given point on that property, and from it are run the openings or roadways, as they call them, the main drifts, and from them the spurs or laterals. As soon as that mine is extended under the ground by its little railways to a point where it would not be economic to bring the coal back from a distant point to the main shaft it would be more economic to develop distant property by sinking another shaft and running other openings, and the mine that was first exhausted by the process, its tipples, its hoisting machinery, and other paraphernalia that goes to mines, would be, of course, nothing but junk, and could be sold at whatever it would bring in a secondhand market.

A sawmill is precisely that operation, only on top of the ground instead of below the ground. A sawmill is constructed often at a very high cost of several thousands of dollars. From time to time logging roads are extended into the forest tract that has been blocked off by the sawmill enterprise, and from that main logging road the spurs extend on either side into the timber as the logging road is projected. There comes a time in that operation when it would be more economic to build another mill and construct another plant than to operate from the original plant that I have just described.

Senator NUGENT. Why can you not move the plant?

Mr. BOYLE. You can not move a sawmill plant in the sense—you can not move it as you could any other piece of property. If you did so you would have to do it at a very great expense.

Senator NUGENT. There is merely the expense of dismantling and moving the machinery.

Mr. BOYLE. All right. We would be perfectly willing. The buildings, of course, would have to be torn down and they would have to be conveyed. Of course, the question of getting the material of the old mill to the new plant is a matter of some moment, but ever since the sawmill business has been in operation it has been recognized that as each thousand feet of lumber is cut that mill property is worth just that much less, and each year—

Senator NUGENT. Are you speaking generally now, or do you mean the mill at that particular point?

Mr. BOYLE. I am speaking generally of the sawmill business. I am not speaking of sash and door and blind mills or woodworking plants, which are continuous operations. I am speaking of a sawmill operation that is a destructive operation, the same as a mining operation, the same as oil production is a destructive operation; because when the oil is gone or the timber is gone or the mineral is gone, the improvements of that operation are nothing but secondhand material. Any man familiar with the problem must recognize that to be the fact, and what we are asking for here is that the same

treatment be given the sawmill operation as is given the mineral and coal mines and oil wells and other destructive enterprises of that kind. To do otherwise, gentlemen, would be to make discrimination. The law recognizes this principle here in those industries, not only as to those natural-resource industries that I have just called attention to, but as to those natural-resource industries that are referred to for war purposes in section 8. If there are any questions, I will be glad to answer them, because it is an important matter; it is going to mean a great deal to this industry. And this statement is made in the utmost good faith. It is not made for the purpose of escaping taxation. We are not complaining of the tax, but we are complaining of the elimination of this national resource as distinguished from others.

The CHAIRMAN. You would have no difficulty in removing the machinery in your mills, would you?

Mr. BOYLE. No, sir; you could remove your machinery.

The CHAIRMAN. And you would have no difficulty in removing the iron rails of your logging machinery?

Mr. BOYLE. And for just whatever they were worth; the tax would get the credit for that.

This matter has been up before the Treasury Department, and here is the suggestion they made under the law as it stands, and this, I think, answers the point that is made: In reply to an accounting showing that was made by a sawmill under the present law, wherein they had followed the practice which all sawmills have followed from time immemorial, of charging off a certain amount per thousand feet to take care of the amortization of the plant, the Treasury Department said: "You can not do this until the last year of your operation. Then you can charge or take credit from the profits you make in the last year for such loss as may have occurred to you due to the fact that your capital could not be returned and that you had not realized your capital from any sinking fund."

The difficulty about that is, of course, that in the last year of a cut of 15 or 20 years there would not be sufficient return in the way of an income to take care of that. And so far as salvaging the machinery is concerned, in salvaging the wire rope, in salvaging the rails, whatever credit there is to accrue to the tax on that matter is taken care of by the administration of the matter by the Treasury Department.

This matter will be looked into and covered in the same way as the peculiar conditions that exist in the zinc mining at Joplin, where a mine is exhausted in 5 years, or a coal mine in Cherokee County that will be exhausted in 35 years. In a lumber operation the depreciation would not be as great, and the loss would not be as complete; but there will be some complete loss there to the owner, and that is a matter for rules and regulations of the Treasury Department. But the principle ought to be recognized, gentlemen, in the bill, under the same idea that is here indicated, "such reasonable allowance in all the above cases to be made according to the peculiar conditions in each case and under rules and regulations to be prescribed by the commissioner with the approval of the Secretary."

So that I do not see where there could be any danger of a loss, of a sawmill getting too much of an advantage, and surely, under the

statement I have made here there is some merit to the suggestion that when the timber is cut out the mill as such, as to that going operation, is a dead thing.

The CHAIRMAN. And that you mean without reference to whether the lumber mill owns the land or leases the land for a given period?

Mr. BOYLE. It would not be material as a lumber operation. That is the thought that I wanted to suggest.

You will notice on your pad there, Mr. Chairman, that my name is mentioned with the names of others. Mr. Holmes, of Kansas City, is here, and I would be glad if you would give him the privilege of presenting another matter which is entirely apart from the matter I have discussed.

The CHAIRMAN. In a sawmill, a well-equipped sawmill plant, what is the proportionate relation of the machinery to the wood construction or the necessary buildings in which to house the machinery and operate the plant?

Mr. BOYLE. Well, I would not be qualified to state that.

The CHAIRMAN. I realize the fact that if you were compelled to move your plant—probably your buildings would be of very little value—would be almost a loss; but your machinery would be of very considerable value.

Mr. BOYLE. Yes, sir.

The CHAIRMAN. In my country—I do not know how it is in your country—but in my country in many cases the buildings are very crudely constructed, very crudely built, and outside, probably, of the drying plant, of very little value. At the end of 10 or 15 years, the period that you say is generally required to cut over a tract of land, they would be of practically no value in many instances. They themselves would be about exhausted.

Mr. BOYLE. I have seen a good many mills in your country, Senator, of course, and I am more familiar with those in the South and in the Lake regions. I do know that these mills that are now built for operation under these modern conditions of high-power machinery are built in these days very substantially. They are not simply boards tacked together; they are real buildings.

The CHAIRMAN. I said many of the plants. What you say is true of some of the larger mills.

Mr. BOYLE. Yes, sir.

The CHAIRMAN. For instance, some near my town; very expensive mills. Their buildings are of a high class. But all through the country, out in the woods where these mills are established, the structures are very crude.

Mr. BOYLE. Yes, sir; depending upon the type of operation that it is. There are what we call the little "tin pot" mills, as you have heard the expression; movable affairs that just have a little shack. But we are not talking about mills of that kind. I am talking about mills that have hundreds of thousands of feet of production to-day and that are built substantially, and where there will be a substantial loss.

Now, I know this committee, if I speak on a matter that has merit—and I assure you that that is my thought, my understanding about it—if the loss is substantial in the event that the timber is cut out, will consider that; and, mark you, a man can not move his mill to

another piece of timber that he wants to cut, because he buys his timber for that one operation. He does not own timber that he can have his mill moved to.

Could I have this privilege, of submitting for this committee's opinion a statement from a practical man as to the relative value of the mill properties, by and large, as distinguished from the machinery, the saws and things of that kind, which we know would be of value, that can be sold in the market. Mark you, they would not be used for another operation by that man; they would have to be sold to some one else as second-hand material for whatever they are worth, and he ought not to be charged with any greater amount.

The CHAIRMAN. I am not meaning to say that there is not a great deal of merit in your suggestion; but this is the situation in the country, as I understand it: A great mill company, owning many hundreds of thousands of acres in some instances, is located at some central point. They have a logging road running into this body of timber and into that body of timber. These logging roads haul all of their production to the main mill, and it is there manufactured. They cut over one tract and they do not tear up that mill and throw it away, but they have another tract to cut over with that same mill.

Mr. BOYLE. Surely.

The CHAIRMAN. And then they have another tract when they get through with that, and the same mill is engaged in cutting over these several tracts for an indefinite period.

Mr. BOYLE. We cut with a mill until the supply is exhausted.

The CHAIRMAN. That may be many, many years; and in that country very frequently they own the tract of land, and reproduction sets in and by the time they have cut over the entire tract there is another crop ready for them on the part that was first cut.

Mr. BOYLE. May I have the privilege of filing a memorandum with the committee?

The CHAIRMAN. Yes.

Senator LODGE. Where they have adopted economic methods of cutting forests, they do not do it as you apparently do it, and it seems to me your idea is drawn from rather wasteful methods of work. It will take 40 years for the time necessary to reforest for the purpose of cutting, and they begin to cut a tract and then move on gradually until they get to the 40th division and then they come back and begin again, and treat it just like any other growing crop, and they move their sawmill about. Now, that is done by some very great companies. I have in mind the Great Northern Paper Co. They never think of charging that to anything more than to ordinary operating expenses.

Mr. BOYLE. The character of the timber that they are operating in makes a difference.

Senator LODGE. The Great Northern Paper Co., of course, is operating in pulp wood.

Mr. BOYLE. That which you are speaking of would not be applicable to the chairman's region or to the southern producing mills.

Senator LODGE. You can not grow oaks in a few years.

Mr. BOYLE. Or yellow pine.

Senator LODGE. They grow pines pretty well in 40 years.

Mr. BOYLE. They can not do that with yellow pine.

Senator LODGE. They can with pine in Maine.

Mr. BOYLE. If you are in wood that is available to the same operation, of course, you can do that.

Senator LODGE. In Maine they grow pretty good pine.

Mr. BOYLE. Yes; but I am talking about a practical, going situation that is here and is an absolute fact, and these mills cut out in 15 or 20 years, and the mills is a loss, comparatively speaking; and they ought to have an opportunity under any bill to be treated the same way that a man is treated that is similarly situated.

The CHAIRMAN. If a company owned just one good-sized tract and had the right simply to cut the standing timber within a certain period of time, and they built a mill upon that tract and they had logging roads to bring in the material, what you say would happen in that particular case, undoubtedly. At the end of the first cut-over their mill would be of practically no value except for the machinery, which would be salvaged, and the iron in the rails which could be salvaged.

Mr. BOYLE. That could be administered by the Treasury Department—and no loss of revenue can come to the Government—according to the facts of a peculiar situation. I would be very glad if you would permit me to file this memorandum.

The CHAIRMAN. File your brief.

Mr. BOYLE. Thank you.

(The brief referred to is here printed in full, as follows:)

NATIONAL LUMBER MANUFACTURERS' ASSOCIATION,
Chicago, Ill., September 23, 1918.

In re deductions allowed in H. R. 12863.

To the Hon. F. M. SIMMONS,

*Chairman, and Members of the Senate Finance Committee,
United States Senate.*

GENTLEMEN: On Monday, September 16, I presented to your committee some observations on subdivision (c), commencing at line 24, page 38, and this in reference to the status of lumber manufacture as to deductions allowed, as such operations may in principle resemble mines, gas and oil well operations.

Subdivision (c) as it stood in the bill when I appeared before your committee read as follows: "In the case of mines, oil and gas wells a reasonable allowance for depreciation of improvements," etc. I urged that "timber and other natural resources" be inserted after the word "wells" on line 25, so that (c) as amended would read: "In the case of mines, oil and gas wells, timber and other natural resources a reasonable allowance for depreciation of improvements," etc.

Since appearing before you the Ways and Means Committee of the House inserted the above language in (c). Thus the bill will come to the Senate committee amended as urged to you Monday.

Due to my own limitations I fear that I did not make my thought clear when before your committee. Permission was given me to file a written statement to supplement the oral argument. I am glad of the opportunity, for I feel confident that the Senate committee will agree to my suggestion once its facts are understood.

Generally speaking, as originally placed in the House bill, (c) was designed to take care of the following situation: Improvements necessary for a coal mine operation, for instance, are of no value (other than as salvage) after the coal is exhausted. The application of the rule of depreciation by wear and tear as applied to business operations generally would not suffice to recover to the coal producer the capital invested in necessary improvements, hence the bill recognized the need of an annual "reasonable allowance for depreciation

this under regulations prescribed by the commissioner with the approval of the Secretary.

The committee is familiar with the ordinary development of a coal property. A shaft is sunk, and from the shaft extends roadways or openings. From these main roadways other openings are made, and in this wise the underground workings are developed. As the enterprise is started with but one object, to wit, the recovery of the coal embraced within the property limits of the particular operation, when the coal is exhausted the improvements are only of such value as can be secured for them as junk or second-hand material. The improvements, as such, are of no value whatever to the exhausted property.

There is one other phase involved in a coal property—there must be a sufficient area to be developed to justify putting in place the improvements. As each ton of coal is taken from the body of the mine the improvements depreciate in value proportionately and when the last ton is lifted the value of the improvements is, as stated, what they will bring as second-hand material.

Lumber manufacture is identical, as to the matter indicated, with coal mining. The only difference is that ore development takes place below the surface and the other on the surface.

A modern lumber operation must first secure a block of timber sufficient to run a mill plant for from fifteen to twenty years. The investor is not justified in erecting the plant until he has not only first secured his timber or raw material supply, but he must secure a sufficient quantity of timber to justify his plant investment. When sufficient timber is secured and the plant erected, logging or tram roads must be extended into the timber. As the timber is cut the railroad is extended farther and farther. Thus the development continues until all the timber has been cut. When this occurs the improvements, to wit, mill, logging roads, dry kilns, etc., are of no further value as such. Their sole value is such salvage as may be obtained.

As in coal mining, with the first thousand feet cut the improvements, as such, depreciate proportionately, and when the last thousand feet is cut the improvements are of that value that they will bring as secondhand material. Because of this fact, expenditures for maintenance in wasting industries should not be charged against depletion in the same manner as they would be charged against depreciation in those industries whose lives are practically perpetual.

Without taking further space as to the fact that when the timber for a given operation is exhausted the plant improvements are of no further value as such, I will briefly address myself as to the character of these improvements.

During the discussion of this matter before the committee the suggestion was made by members of the committee that these improvements were rather inconsequential and could be easily moved. As to this latter suggestion, I feel that I have made it clear that there is no place to move the plant after timber is cut from a given operation. That is to say, a man who has blocked out 15 or 20 years of timber, when he has cut it he is through. If there is other timber adjacent that he can buy and economically cut with his plant as erected, of course he will purchase such timber. However, in the South, for instance, practically all of the available tracts are now under operation or blocked out for a new plant. If a man who has cut out one block has another block of timber to cut some place else, true he could utilize a part of his old plant in the new operation, but he can not move his plant, as such, to the new operation—he must rebuild and reconstruct the new plant. For just such value as the old material would have in the new plant he should credit capital account on the old operation. An instance of this kind would be the exception and not the rule, and in addition the situation would always be within the control of the department, whereby rules would be laid down governing all such phases.

As to the character of improvements that designate a modern sawmill, I feel that I can best illustrate this item by attaching hereto and making same a part of this presentation, two letters written me from clients at Kansas City in answer to a query from me which was based upon suggestions made by the Senate Finance Committee at the hearing above referred to. These letters, with the data attached, sufficiently explains the character of a modern sawmill.

In passing, it is but fair to state that the plant referred to in this letter is a very moderately sized plant as compared with such plants as the Great Southern, at Bogalusa, La., and many, many other operations.

Accompanying this statement I am filing with the secretary of the committee photographs of the mill plant referred to in Mr. Keith's communication. I thought the photographs themselves would rather illuminate the presentation and bring before the committee in a vivid way the fact that these improvements

are not only extensive but quite substantial. In addition I am handing the secretary the ground plan of the Conroe mill, which plan will indicate to the committee the extensive character of a modern sawmill plant.

I would like to have the privilege of withdrawing the photographs and the ground plan after the committee has examined same.

I trust that when the House bill comes before the Senate committee and item (c) comes under review that the committee will have in mind the suggestions here generally indicated, so that there will be a correct grasp of the thought that lumber manufacture is a wasting industry, as is coal mining and other mineral operations, and plant depletion must be treated in the same way as in mines, gas and oil wells. Any other method would simply deprive lumber manufacture investment of a full return of capital investment in improvements and which return is accorded to all other industries.

Very respectfully,

L. C. BOYLE

P. S.—Senator Lodge made the suggestion that in Maine the pulp operators moved their plants from time to time and their growth of timber was made available to such plants. This suggestion would not at all apply to the character of timber that comes within the scope of lumber manufacture, generally speaking. Southern pine and fir timber takes a century to mature. The life of an ordinary sawmill operating in such woods would in no wise enable a second growth to be available. Further, even if the principle was applicable, such fact would come properly within the purview of the Revenue Department's regulations as provided by the bill.

CENTRAL COAL & COKE CO.,
Kansas City, Mo., September 17, 1918.

Mr. L. C. BOYLE,
624 Southern Building, Washington, D. C.

DEAR SIR: Referring to the attached statement of the cost of construction of the Conroe (Tex.) plant:

Owing to a lack of time we can only analyze a few of the large items on this statement. We have taken the sawmill and sawmill power house and the planing mill and planing-mill power house and are giving you below a statement showing the total cost of these parts of the plant and then showing the cost of the machinery on these parts of the plant:

SAWMILL AND SAWMILL POWER HOUSE.

Sawmill.....	\$99,858.69	
Power house.....	54,065.78	\$143,924.47
Sawmill machinery.....	32,307.16	
Power-house machinery.....	33,962.89	66,270.05
Total.....		77,654.32

Machinery approximately 46 per cent of total cost.

PLANING MILL AND PLANING-MILL POWER HOUSE.

Planing mill.....	\$46,992.28	
Power house.....	19,976.45	\$66,968.73
Planing-mill machinery.....	18,994.01	
Power-house machinery.....	10,477.59	29,471.60
Total.....		37,497.13

Machinery approximately 44 per cent of total cost.

You will notice that the machinery is approximately 46 per cent of the total cost of the sawmill and sawmill power house and that the machinery is approximately 44 per cent of the total cost of the planing mill and planing mill power house. The portion of this investment shown as machinery is the only part that would have any salvage value when the plant is cut out and it would

probably bring 50 cents on the dollar, and that is a liberal estimate under normal conditions. The buildings, the labor, and material going into same and all items of expense of that character making up the investment would be worthless.

Yours, truly,

CHAS. S. KEITH, *President.*

CENTRAL COAL & COKE CO.

Kansas City, Mo., September 17, 1918.

Mr. L. C. BOYLE,
Washington, D. C.

DEAR SIR: Replying to your wire, I am inclosing herewith exhibits in connection with the total investment in our plant at Conroe, Tex., being statements and photographs in connection therewith, the photographs showing views taken both during construction and as the plant stands at present time. This will serve to give you an idea of the character of construction necessary for a plant of this nature. It may be necessary for you to keep these photographs, but I hope you will not, as I would like to have them returned to me, especially those in the album.

(1) Below I give you statement of analysis of the capital invested, and the distribution thereof, of 96 southern pine companies, operating more than 100 mills and producing 4,445,648,000 feet annually, which is more than 25 per cent of the total production of southern pine. These companies had a total investment on December 31, 1917, of \$270,349,000, distributed as follows, to wit:

Investment in timber (60 per cent of the total)-----	\$162,917,000
Investment in plant (18 per cent of the total)-----	49,137,000
Accounts and bills receivable, stocks of merchandise, and inventories (approximately 18 per cent of the total)-----	49,791,000
Miscellaneous assets (approximately 4 per cent of the total)---	8,504,000

In other words, 78 per cent of the total investment necessary for the conduct of the business was of a nature which depleted itself.

These companies had 32,053,744,000 feet of standing timber, with an investment therein of \$5.08 per M feet; in plant, \$1.53 per M; in quick assets, \$1.55 per M; and in miscellaneous assets 27 cents per M, or a total of \$8.44 per M. As the timber is cut \$5.08 is expended for timber and \$1.53 for plant, or a total depreciation of \$6.61 per M.

From the foregoing you will see the amount of money necessary to establish a plant. Most sawmill propositions have not only the question of plant to consider, but the question of town site, millhouses, commissaries, stores (not stocks), and all the improvements which are necessary for the purpose of taking care of and housing the employees of the industry, which, when the lumber is cut, immediately become of no value, not being worth enough to justify wrecking them and moving them to some other point. Houses costing \$700 to \$1,000 have frequently been sold under such conditions for \$25 and \$30 each.

(2) I am inclosing a statement showing the investment in the Conroe plant, and direct your special attention to the fact that the railroad includes only the right of way, the ties, and the dump, but not the steel, which is rented. It is obvious this item will be of absolutely no value when the timber is cut. This plant cost over \$800,000 in 1914, at a time when materials which went into its construction were at the lowest price in history, but under normal conditions the entire equipment of the plant if wrecked and placed upon the market would not bring over \$100,000. Of course, such a plant would bring more under present abnormal conditions.

(3) I inclose a map showing the location of buildings on the mill site, and in lead pencil I have noted the cost of each division of this plant. I call your special attention to the fact that it cost us \$11,015.71 to get two artesian wells put down, and the casing in them can not be extracted. They have no value whatever, except as a source of water supply for the plant and fire protection therefor.

(4) I also inclose you a book of photographs taken during construction of this plant, which show the character of its construction. In addition, I hand you a number of photographs showing present condition of the plant, on the back of which is noted the items shown in the investment statement.

Yours, very truly,

CHAS. S. KEITH, *President.*

Delta Land & Timber Co.—Cost of construction—Conroe Plant.

Sawmill:		
Sawmill	\$99,858.69	
Green lumber sorter	15,293.40	
Sawmill power house	54,065.78	
Sawmill fuel house	4,970.99	
Artesian well	11,015.71	
Machine and blacksmith shop	15,167.98	
Electric lights	7,585.50	
Lath mill	5,566.42	
Log pond	5,780.32	
		\$219,304.79
Housing for employees:		
Houses		29,351.38
Office expense		193.19
Yarding:		
Dry kiln and platform transfers	26,708.60	
Dry kiln	58,896.11	
Rough lumber shed	16,744.44	
Dry lumber sorter	22,452.66	
Overhead trolley system	43,634.42	
		167,936.23
Logging:		
Walker County Railroad	156,220.08	
Logging equipment	102,338.37	
Railroad	2,909.82	
Wood houses	7,360.01	
Woods store	898.86	
Railroad motor car	1,963.43	
Truck scale	2,099.35	
Telephone line	554.87	
		274,344.79
Waterworks:		
Water system		16,984.90
Planing and loading:		
Planing mill	46,992.28	
Dressed-lumber shed	11,756.47	
Planing mill power house	19,976.45	
Loading platforms and dressed-lumber sheds at planing mill	10,587.84	
		89,313.04
Miscellaneous:		
Temporary mill barn	90.80	
Cleaning mill site	1,383.73	
Personal property and fixtures	489.82	
Live-stock account	1,757.16	
Plant warehouse	775.40	
		4,497.01
General expense:		
Administrative expenses during construction		23,914.51
Total		\$825,839.71

STATEMENT OF MR. MASSEY HOLMES, REPRESENTING THE PINE ASSOCIATION.

Mr. HOLMES. Mr. Chairman and gentlemen, I represent the Pine Association, which represents the manufacturers of yellow-pine lumber in the South. I shall address myself to the question of defining "invested capital" in section 226 of the bill.

Will you kindly assume, gentlemen, this illustration for the purpose of my discussion, that there are two lumber-manufacturing companies, each with assets of identical value, say \$200,000, each during

the taxable year with operating expenses of precisely the same amount, each during the taxable year with an income of the same amount. Given those conditions, our contention is that those manufacturers are similarly situated, and under any principle of equal and just and fair taxation any tax on the incomes of those two respective companies should be the same.

Our taxes under these revenue laws are all taxes on the incomes of those two companies. They are called in one instance, of course, the normal tax, in another instance an excess-profits tax, and in another a war-profits tax, but each tax is a tax against the income of the business; and we say and urge that, given a property of the same value devoted to producing an income, given the same net income for the companies A and B, the taxes ought to be the same.

Senator SMOOT. That is, if one company, A, was run at a loss and company B was under better management and made 100 per cent. company B should not pay any tax?

Mr. HOLMES. Yes; precisely; if A made \$100,000 and B a net income of \$100,000, the tax should be the same.

Senator SMOOT. It would be the same in that case.

Mr. HOLMES. It should be.

Senator SMOOT. It would be under the situation you present; but there are a thousand cases where it would be and there are 10,000 cases where it would not be.

Mr. HOLMES. The 10,000 cases where it would not be make an unequal taxation, it seems to me.

Senator SMOOT. Yes; but not the case you presented. Your proposition is entirely different from that.

Mr. HOLMES. No, sir; I had not gotten to a point where you could definitely say that it was or was not different. All that we have now is the property, valued at \$200,000, with a net income of \$100,000 in each case.

Senator SMOOT. Yes.

Mr. HOLMES. Now, it does not follow that the tax under the revenue laws is going to be the same in each case because the available capital, the invested capital, as defined in the present law and the proposed bill is the same.

Senator SMOOT. When you started out, of course, I understood you to say that the capital was the same.

Mr. HOLMES. No, no.

Senator SMOOT. Well, the other, of course, there is no question about at all. We have had dozens speak of it, and we all know it. There is no question but what there is a discrimination under the provisions of this bill.

Mr. HOLMES. Do you think it ought to be remedied?

Senator SMOOT. I do; and I am going to try to do it; but I do not know whether I can or not.

Mr. HOLMES. Then, I do not know whether there is any use of my presenting that further.

Senator SMOOT. The committee knows that thoroughly.

Mr. HOLMES. The committee knows that under the present law and proposed bill the manufacturer of lumber may have returned to him, net, less than the actual present-day cash value of the stumpage which he consumes in its manufacture?

Senator SMOOT. That all depends upon the price he sells his lumber at.

Mr. HOLMES. The Federal Trade Commission has recently said that the cost, exclusive of the value of stumpage, average, is \$18 a thousand. It is generally understood that the value of stumpage on March 3, 1917, which, of course, you must use in computing your income tax, was \$5 a thousand in the South. That would make a total cost of \$23 average. The price-fixing committee of the War Industries Board has recently fixed \$28 as a fair and reasonable return to the manufacturer. That leaves a margin of profit there of \$5 a thousand. The stumpage is actually worth to-day from \$7 to \$8. Now, if you compute invested capital on original costs instead of on the value as of March 3, because none of us consider that the war inflation should be considered, if you take the original cost, your manufacturer may get in 60 or 70 per cent, and of that he pays \$3.50, leaving \$1.50 a thousand which, added to the \$5 he may deduct in computing his income makes \$6.50, which is less than the \$7 or \$8 his stumpage is actually worth to-day, leaving him a loss on that, under which he can not carry on, and making a loss of revenue to the Government.

Senator LODGE. In the case of your two companies, they originally cost \$100,000?

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Mr. HOLMES. Yes; to everything; because I think it is not impracticable—the administration, either—because we have all got to determine the value as of March 1, 1913, in determining whether we make or lose property in disposing of it.

The CHAIRMAN. I am advised that Mr. Andrews is here with a delegation, and he wants to be heard about five minutes.

Mr. ANDREWS. Yes, sir

STATEMENT OF MR. JESSE ANDREWS.

Mr. ANDREWS. I am a lawyer and reside in Houston, Tex. My firm is counsel for the Long-Bell Lumber Co., of Kansas City, Mo.

Mr. Chairman, I wish to speak particularly with reference to the effect of the proposed bill upon stock dividends that have been previously declared. That may be a subject that has received the attention of the committee heretofore—if so, I am not advised of it—the effect of the proposed bill on the income of stockholders who have received stock dividends declared this year; but prior to the introduction of the proposed bill.

Senator SMOOR. You are opposed to the restrictive features of it?

Mr. ANDREWS. Yes, sir. I shall limit my discussion to stock dividends, and also to stock dividends declared prior to September 3, 1917, for the fact is that in the early part of this year the companies of which my firm are counsel declared and paid a number of stock dividends, the stockholders thinking that the tax which would be assessed on account of the stock dividends would be based upon those rates which were applicable during the years in which the earnings were accumulating which were distributed by these stock dividends. They would not have voted for the stock dividends if they had for a moment thought that that plan of taxing stock dividends would be changed so as to make the dividends not only a part of the income for this year but also taxable at the rates which would be promulgated for the year 1918.

Senator THOMAS. In other words, you assumed, and had a right to assume, that the Government which you were supporting would not further impose a retroactive tax?

Mr. ANDREWS. Yes, sir; that was it. It was not as though we were assuming that the rates would be the same, because it was not that. It was a question of principle or policy.

In passing the 1917 act, as you gentlemen will remember, you provided then that it would not be permitted to corporations thereafter to fix the years or the earnings out of which the dividends would be paid, but that automatically, if I may say, the dividends would be deemed to distribute those earnings which were most recently accumulated. If the dividends were paid in the spring or in the early part of 1918, before any dividends for that year had been accumulated, those dividends, regardless of the wish of the corporation, would be deemed to distribute such earnings as had been earned in prior years, but which had not been distributed.

But you provided also in that act for this, and this is the important thing and is the thing which guided these gentlemen in voting for the stock dividends: You provided that while the dividends would be distributed in the way I speak of, and while they would

constitute a part of the income of the taxpayer of the year in which they were received by the taxpayer, they would be taxable at the rates prevailing during the years in which those earnings were accumulated by the corporation. Now, that was the situation which confronted these companies in the spring of this year. They naturally anticipated that there would be an increase in rates, because all recognized that more money would be required; but they thought that the plan that had been set forth with respect to the stock dividends was that they, when received, would be taxable in the hands of the stockholders at the rates prevailing during the years in which the earnings were accumulated. They knew in the spring of 1918 that these stock dividends which they were about to declare distributed earnings of prior years and not of 1918, and they voted for the payment of the stock dividends. Now we find that if the proposed bill becomes a law, those dividends become a part of the income of the stock holders this year, and instead of being taxable at these relatively low rates, which was understood when the dividend was declared, they are taxable at the very high rates.

If I may be permitted to give you the figures in the case of one stockholder, it is really astounding—a stockholder who was a manager of one of these mills, who in his long connection with it in years had invested his earnings in the stock of the mill, and the earnings having been retained in the business, which earnings, together with this increase in value which Mr. Holmes has spoken of causing a very large increase in the book value of the stock over and above its par value, he received dividends amounting, in stock, to \$179,000.

Senator THOMAS. Last year?

Mr. ANDREWS. He received them in the spring of this year, before there was any suggestion of a change.

Senator THOMAS. Yes; and out of the earnings of other years?

Mr. ANDREWS. Out of previous year, running back to 1902, and running up inclusive to 1913; earnings of past years. Now, he expected to pay and was willing to pay, a tax of about \$25,000—

The CHAIRMAN. Had they declared those dividends—had they declared any dividends from the earnings of this year?

Mr. ANDREWS. No, sir; I think not. The dividend declared at this time was intended to distribute such earnings as had been accumulated in 1918 and, retrogressively, back to the beginning of 1913.

Senator SMOOT. Do you remember the date that the dividend was declared?

Mr. ANDREWS. It was in April, 1918.

Senator SMOOT. Was that your quarterly meeting of the directors?

Mr. ANDREWS. It was the annual meeting.

Senator SMOOT. And the report was made for the year 1917 business?

Mr. ANDREWS. Yes.

Senator SMOOT. And it was upon that report that a stock dividend was declared.

Mr. ANDREWS. I am not sure but what the report came down, and recognizing that the dividends accumulated in 1918—the profits, if any, accumulated in 1918—had to be distributed also, I am not sure but what it included also such profits as had been accumulated from the 1st of January, 1918, down to the date of the dividend.

Senator SMOOT. Is that the end of your business year, January 1?

Mr. ANDREWS. January 1 is the end of the business year, but the annual meetings are held about the time I speak of.

Now, this gentleman expected to pay a tax out of this stock dividend, which, based upon the rates of the preceding years, would have amounted to about \$25,000. His tax now, he finds, if this bill should become law, would be \$83,437. This law will result in a tax to him on account of his stock dividends alone of some \$57,767. In the language of the Supreme Court of the United States, with which you gentlemen are familiar, he was no richer after the declaration of that dividend than he was before. I refer to that principle as to stock dividends just to show what an enormous rate he would be paying, some \$57,000, if this bill should become a law, for the purpose of having—

Senator THOMAS. I have never been able to accept that decision of the Supreme Court as logical; but I think you are quite right in complaining against a retroactive tax.

Mr. ANDREWS. I was just going to say, Senator, whether that is strictly true or not, or strictly accurate or not, there is not an amount there commensurate with this greatly increased sum of money.

Senator THOMAS. I agree with you on that.

Mr. ANDREWS. Now, it seems to me that can be readily remedied by adopting the language taken from the act of 1917, and inserting it on page 4, line 15, after the word "distributed"; and if I may, I will continue with the reading; I will read the whole as it would be. On page 4, line 15, insert after the word "distributed" (changing the period at that point to a semicolon) the following: "; shall constitute a part of the annual income of the distributee for the year in which received, and, as to such stock dividends declared and paid prior to September 3, 1918, shall be taxed to the distributee at the rates prescribed by law for the years in which such earnings or profits were accumulated by the corporation."

The CHAIRMAN. You want that particular provision written into the present law?

Mr. ANDREWS. Yes, with respect to these dividends that have been paid prior to September 3. The committee will remember when you introduced that law last year you adopted that practice yourself, of making its application not retroactive beyond the date when the Senate report was introduced, which was August, I think, 1917.

With the permission of the committee I should like to say just one word on another subject. It is a subject that Gen. Boyle referred to and I will speak of it in the briefest way only, because I would like the committee to know what the situation is with respect to the yellow pine sawmills in Louisiana and Texas, among the largest of which are lumber mills which we represent and in connection with which I would like to file just a memorandum.

The situation there as I understand it is that these mills, each company for itself, first locate a large body of land. They build a mill that is commensurate with the size of the body of land, and I think that the information we will furnish the committee will show that those mills are very substantially built and involve a substantial outlay of money, and are built with considerable attention to stability and permanency.

The companies I speak of anticipate the best they can what will be the salvage value of that mill at the end of the cut, assuming that it is kept in a state of constant repair by repairs and renewals which are charged as a part of operating expense. They assume what will be the salvage value of that plant after the expiration of the cut. They arrive at a certain number of dollars, forming about 80 per cent of the cost of the plant. They divide that number of dollars by the number of feet of standing timber which will be cut during that time, arriving at a unit value of so much per 1,000 feet. Now, as that timber is cut that unit value of so much per 1,000 feet is added to the cost of manufacture and is set up in what is called a depreciation reserve, the purpose of that reserve being to furnish at the end of the cut a fund which, together with the residual value of the plant, will restore the original value of the plant. That is the practice which they have followed uniformly up to this time, and the practice which they would like to have supported by the amendment which Gen. Boyle has suggested.

The CHAIRMAN. I want to say to the committee that Mr. Charles Piez, vice president of the Emergency Fleet Corporation, has written me—that is, he did not write the letter himself, but Mr. Hurley wrote me a letter—in reference to Mr. Piez submitting to the committee some views that he thought, without indicating what they were, might be of value to the committee. I received that letter Saturday, and I wrote him at once that we might possibly close the hearings to-day, and if it was possible he could come to-day; and if he could not come to-day, probably the committee might hear him at some later time. He is not here. He either did not get the letter—

Senator SMOOT. We could hear him any time this week, I should think.

Senator THOMAS. Mr. Chairman. I was informed by some gentleman representing the mining industry, Mr. Callbreath and Mr. Armitage, of New York, that they wished to be heard for a few minutes upon the amendment that Mr. Callbreath proposed. I do not know whether they are here or not.

The CHAIRMAN. These hearings are to go over until to-morrow, because some gentleman wired us that this was a Jewish holiday, and asked if he could be heard to-morrow, and the committee directed me to wire him that he could be heard to-morrow.

Then, Mr. Vanderlip wished to be heard to-day, but he missed his train and would not be able to get here until late this afternoon, and we agreed also to hear Mr. Vanderlip to-morrow; so that we can hear this other gentleman also, I think, if he gets here to-morrow.

Mr. Rush C. Butler will be heard at this point.

STATEMENT OF MR. RUSH C. BUTLER.

Mr. BUTLER. Mr. Chairman and gentlemen, I appear on behalf of the National Coal Association, composed of about 2,000 members, about one-half of whom are local coal associations. Their tonnage is confined to bituminous coal and represents about 350,000,000 tons of annual production out of 540,000,000 tons last year.

The individual operating companies that are in this membership are very large—the largest—and very small—the smallest.

We have three or four different points concerning which we wish to speak very briefly. Only one of them pertains to the coal industry independently, and that is not independently of the mining industry, as a whole, and I only venture to suggest that, and that is the added exemption that should be allowed to the mining industry over and above other industries, because of the fact that we were advised by the public press that the Treasury Department had made such a recommendation to the Ways and Means Committee; but we do not find any embodiment of that idea in the present bill.

The reasons for an extraordinary exemption on the mining industry as numerous, but two will suffice at the present time: First, because the mining industry is extra hazardous and only invites capital that is willing to take extra chances, which, in turn, is entitled to a larger percentage of profit; and, second, the extra exemption should be allowed for the coal industry, because of the fact that the coal industry pays a higher percentage of its net profits by way of a Federal tax than any other industry. I can not make this statement, however, authoritatively, but I have been so advised by representatives of the Treasury Department. It would, therefore, seem that if all industries are to be on a comparative basis, there is just occasion for the Treasury Department's recommendation that a special exemption applicable to the mining industry be made.

The next proposition we have in mind is a revision of the definition of "invested capital," and Mr. Hornberger, of the Pittsburgh Coal Co. and the treasurer of that company, the largest bituminous coal company in the United States, is here to speak upon that subject, but I wish to leave with you a brief compilation that has been prepared by one of the members of our committee, Mr. Marion, of Pittsburgh, from reports made to our committee from various of our operating members. This tabulation shows the capital of these reporting companies per ton of annual production, based upon the returns made to the Treasury Department for the purposes of taxation, and it will illustrate better than anything else I know of how unjustly discriminatory as between competitors within the coal industry are the provisions of the present law. The same situation, undoubtedly, exists in other industries, and I may say all other industries, but I have the actual figures here from the coal industry. For instance, we have 41 companies reporting out of a total of 395, whose capitalization per ton of production is under \$1. Their average capitalization per ton of production was 65 cents.

Omitting those up to the \$5 mark and above, we have them under \$1, and between \$1 and \$2, and so on; but omitting those and going to the highest, we have 34 companies reporting a capitalization in excess of \$5, running up in one instance to \$13.93 per ton; an average of \$8.21 per ton.

The story that is told by these figures is simply this, that when the exemption of 7 per cent, if you please, or 9 per cent, whichever it is, is applied, and taking 7 per cent because most of the coal companies did not have prewar earnings equal to 7 per cent, but applying 7 per cent exemption to these companies, the company capitalized at 65 cents per ton would have an exemption per ton of less than 5 cents, whereas the company capitalized at \$13.93 a ton, or practically \$14 a ton, at 7 per cent, would have \$1.28 exemption per

ton of coal. If these two companies happen to be in the same field where the price of coal is the same, you see that the company with the exemption of \$1.28 from taxation is at a tremendous advantage over the company having an exemption of only 5 cents a ton. I will leave this with the committee.

(The paper referred to is here printed in full, as follows:)

Capital per ton production.	Companies reporting.		Their per cent of the production reported.	Capitalization per ton produced.			Exemption on basis of 10 per cent of capitalization.
	Number.	Per cent of total.		Low.	High.	Average.	
Under \$1.....	41	10.38	19.6	\$0.047	\$0.963	\$0.65	\$0.065
Between \$1 and \$2.....	156	39.49	27.6	1.022	1.958	1.43	.143
Between \$2 and \$3.....	105	26.58	21.9	2.00	2.857	2.14	.214
Between \$3 and \$4.....	34	8.61	6.3	3.072	3.979	3.46	.346
Between \$4 and \$5.....	25	6.33	13.8	4.21	4.887	4.65	.465
Over \$5.....	34	8.61	10.8	5.04	13.93	8.21	.821
Total.....	395	100.00	100.0	.....	.....	2.72	.....

Capitalization of companies in first three groups, representing 69.14 per cent of production, is \$1.42 per ton.

Capitalization of companies in last three groups, representing 30.86 per cent of production, is \$5.88 per ton.

Companies reporting produce 143,894,300 tons.

Senator JONES of New Mexico. You mean 65 cents a ton per annum? You mean taking into consideration a year's output?

Mr. BUTLER. Yes; that is, the capitalization for each ton of production for the year 1917, 65 cents up to—

Senator JONES of New Mexico. \$14 per ton, practically?

Mr. BUTLER. \$14; yes, sir.

Now, the other point, that Mr. Hornberger will speak on, is including borrowed capital in capital investment, and the fourth point that we have in mind is the one pertaining to amortization.

Senator JONES of New Mexico. Before you leave this other point, what is the cause of such a great difference in capitalization in those concerns?

Mr. BUTLER. It is not in capitalization, Senator Jones, as such, but it is in the definition of invested capital as it is contained in the act. Invested capital is limited to the amount of stock, the par value of the stock originally issued for property, plus certain items of cash earnings, etc. Now, it happens, perhaps, in the case of some of these companies who have very low capitalization, that they have been running 15 or 20 years, and that they have depreciated their property so that their capital account is very substantially reduced at the present time; and for a company of that kind no special consideration is invited. But, to take Mr. Holmes's illustration, take two companies that have established themselves side by side in the same field—

Senator JONES of New Mexico. It involves, then, a question of appreciation of the value of the coal lands; is that the point?

Mr. BUTLER. Yes; very largely.

Senator JONES of New Mexico. That is what I was trying to get at—what the main element was.

Mr. BUTLER. Yes, sir. Is that all you wish on that point?

Senator JONES of New Mexico. Yes; thank you.

Mr. BUTLER. Then, on this point, we were very much concerned with that subject prior to the time that we knew what the contents of the House bill were to be, because, as I read the testimony of the engineer from the Fuel Administration who was here day before yesterday, he made it very clear that under the law as it stands to-day it is not only difficult but it is absolutely impossible for operators to continue improving their property or even keeping it up to the present standard unless these unusually high war costs can be specially amortized; but we are quite well satisfied with the provisions of the House bill. It seems to us that they might have gone a little further, because a limit of amortization of 20 per cent of the net earnings of any company in a given year is liable not to be any more than 5 per cent of the cost or 10 per cent of the cost, and we think that if you gentlemen can find a way to provide for special amortization of the excess cost, due to war conditions, of these additions and improvements over and above the prewar cost, you can come nearer arriving at justice and permitting the operators to develop and improve and repair and keep up their property than you can under the provisions of this law, which, while apparently on their face very fair, may limit the amortization to a very small percentage of the actual cost of these additions and improvements.

We had in mind originally that subject of adjustment in later years, which would be in the control of the Treasury Department. It might not be improper to allow amortization of this excess cost at the rate of even as high as 50 per cent per year for the period of two years; that is, 50 per cent of the cost, without reference to the net profits of the corporation.

It is true that during the year or years in which amortization is taking place a very considerable saving in taxes, if that is what you please to call it, would be made by the operators; but in subsequent years their excess profits would be tremendously increased, and, of course, we are all prepared to pay these excess profits, not only for the duration of the war but for at least a few years thereafter.

Senator SMOOT. That is, the beginning of the third year—with the third year?

Mr. BUTLER. Yes; with the beginning of the third year. We think that arrangement would be more satisfactory than that contained in the present bill.

Mr. Hornberger has been asked by me to speak on this bill, and he only came in to-day.

The CHAIRMAN. Mr. Hornberger advises me that he would prefer to address the committee to-morrow rather than to-day, and Mr. Owen must appear before the committee now or not at all, because he must leave the city this afternoon. If there is no objection, Mr. Hornberger instead of being heard this afternoon will be given a few minutes to-morrow morning. How long will you want to-morrow morning?

Mr. HORNBERGER. I think 10 minutes will be ample for me.

The CHAIRMAN. I ask that question simply because we are very anxious to get through these hearings by noon to-morrow. We will hear Mr. Owen now.

STATEMENT OF MR. M. J. OWEN.

Mr. OWEN. I will be just as brief as I can. It will not take but three or four minutes. I want to confine myself to section 600. I represent some 18 companies which are engaged in the manufacture of household and veterinary remedies, and also flavoring extracts, spices, and toilet articles, which are distributed almost entirely to some rural communities by means of some 20,000 salesmen and agents, one of whom usually covers a county and calls on some 800 to 1,000 people several times a year.

Section 600 provides for an increase on nonbeverage alcohol, which means, according to letters that I have received from all the companies I represent, an increase of price which will be equivalent to some 40 or 50 per cent upon gross sales of the extracts and medicines, which is substantially the same percentage as is indicated by, I understand, the medicine people and proprietary medicine people, who have appeared here before you. Upon our entire sales, including spices and lubricating oils and things which are entirely disassociated from medicines, it is going to mean a tax of 17 per cent, and our idea is that it is a tax on the raw ingredients which it is absolutely necessary we should use. If there was anything we could substitute for the nonbeverage alcohol, we would be tickled to do it, because the price is so excessive. The prices of other drug ingredients have increased enormously, more than in any other business, and as we must pay the additional revenue we feel that it should be distributed by means of a gross-sales tax, or even of an investment tax.

There are other sections by which we are affected, particularly the 10 per cent consumption tax upon which there was a specific tax last year. That, this year, in the case of our industry, is going to mean an additional revenue to the Government of five to ten times that which they received under the 1917 law.

I do not intend to say a thing about that. If the committee feels that they require from our industry that much more, we will be glad to see that it is made; but we do feel that it is going to mean a serious situation for us in this increasing rate on alcohol. It is going to amount to that extent that we can not get away from it. Our methods of doing business, selling mostly to farmers, many of whom live in sparsely settled communities and small villages, results in their buying ahead. When our men get around only three or four times a year, they estimate for the next two or three months, and if they think they have got a horse that is going to be sick they get some colic medicine. They buy these things in advance and keep them on hand; and if you are going to increase the price of these remedies so greatly, the farmer is going to take a chance and get along without them, and it is going to mean a sharper decrease of sales for us than for other people, and a decrease in sales which we believe so far as our own particular branch of the industry is concerned, will practically nullify the increase in the rate in its result upon the revenue to the Government. In other words, our decrease of sales will result in a decrease in our use of nonbeverage alcohol, which we will not purchase, and with the decrease of purchase by our concerns, and the decrease of individual purchasing among the customers

visited by our 10,000 men, the result will greatly outweigh the additional revenue which you would derive from the increase on alcohol. Of course we stand a little differently there from the general drug trade, but it hits us just as heavily if not heavier than it does them. That is the only point I will take up.

The CHAIRMAN. The committee will now hold an executive session. (At 5.30 o'clock p. m. the committee went into executive session, at the conclusion of which an adjournment was taken until to-morrow, Tuesday, September 17, 1918, at 11 o'clock a. m.)

TO PROVIDE REVENUE FOR WAR PURPOSES.

TUESDAY, SEPTEMBER 17, 1918.

UNITED STATES SENATE, COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 11 o'clock a. m. in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present, Senators Simmons (chairman), Thomas, Robinson, Jones, Nugent, Lodge, McCumber, Smoot, Dillingham, and Townsend.

The committee resumed the consideration of the bill (H. R. 12863) "to provide revenue, and for other purposes."

The CHAIRMAN. We will hear Mr. E. C. Lindley first.

INVESTED CAPITAL.

STATEMENT OF MR. E. C. LINDLEY, OF ST. PAUL, MINN.

Senator THOMAS. To what item of the bill do you wish to direct our attention?

Mr. LINDLEY. I want to talk about subparagraph 2 of section 326.

Senator NUGENT. What interest do you represent?

Mr. LINDLEY. I am here as counsel for the Great Northern iron ore properties, and I am here because that is a trust, and I felt it was my duty to the cestui trustants to appear.

Under subparagraph 2 of section 326, limiting the value of property to the par value of stock exchanged therefore, the properties in the Great Northern iron ore trust would be worth \$1,750,000.

Under paragraph 3 of the preceding section they are to be deemed to be worth \$150,000,000.

Under title 10—the excise tax provision—we pay a tax upon a basis of about \$50,000,000 to \$60,000,000, and it is that glaring inequality, working a very gross injustice, that I felt it my duty to the beneficiaries in that trust to appear and bring to the attention of the committee. I do not think there is any phase of invested capital that I can inform you about. I point out that inequality, and I think it is always bound to work that way if you do not stand by the fact, and I think the fact should be actual value. On actual value, as I say, we are paying a capital-stock tax on a basis of about \$50,000,000 or \$60,000,000, and if it is worth \$50,000,000 or \$60,000,000 for the purpose of a capital-stock tax, the property ought to be worth \$50,000,000 or \$60,000,000 for the purpose of excess profits or war tax. I am not complaining about the amount of taxes you are levying, or the rate, but I say that that is an inequality that ought to be corrected, and I think it ought to be actual value.

Senator SMOOT. The actual value at what time?

Mr. LINDLEY. At the time you are paying the tax.

Senator SMOOT. For the year in which the tax is imposed?

Mr. LINDLEY. Yes. These properties were exchanged some 12 or 15 years ago, and the present owners are not the then owners at all. They are represented by transfer certificates traded in on the stock exchange, so that the present owners are not the persons who were the owners at the time of the exchange.

As a practical proposition, I want to call your attention to another thing. You are levying a very heavy estate tax. I am not saying anything about whether your tax is borrowed or not, but when you get into a large estate, if they had to go through probate and raise the cash to pay the tax, you would bankrupt the estate, because they could not dispose of the properties to get the money to pay the tax. I think you ought to provide that the Government would take, in payment of its tax, securities, and that kind of property which the Government appraises, and take them at the value you appraise them at for the purpose of paying the tax. Otherwise it would be impossible to raise the money without sacrificing the estate.

Senator JONES. Which one of those figures ought to be taken as the basis of your valuation?

Mr. LINDLEY. I said I thought you ought to take the actual value at the time of levying the tax.

Senator JONES. How are we going to ascertain that?

Mr. LINDLEY. That is a thing you have to ascertain in many cases. You have to do it by the best evidence you can get. As a matter of fact, we have returned to the Government, under the capital-stock tax, a value of between \$50,000,000 and \$60,000,000.

Senator JONES. Is that property being worked at the present time to its full capacity, or anything like it?

Mr. LINDLEY. A very considerable portion is being worked. It is mostly under lease to large steel companies, which consume the ore themselves. In so far as that which is not under lease is concerned, we are trying to negotiate leases.

Senator JONES. What percentage of output have you, compared with the quantity of ore in sight?

Mr. LINDLEY. The total quantity of ore estimated to be in the properties is somewhere around 400,000,000 tons. Just the total tonnage being produced by all our lessees I can not tell you, but it is several million tons—perhaps three or four million—a year. There are different companies which have leases.

Senator JONES. At that rate you have a supply there which would last a hundred years.

Mr. LINDLEY. The leases all call for a graduated increase, and, as it has been estimated, it will take 30 to 40 years to exhaust it.

Senator JONES. What would be the basis of value of that kind of property?

Mr. LINDLEY. They have figured out present value for taxation purposes in Minnesota, and on the basis of the present value of the ore in the ground these properties are worth about \$50,000,000.

Senator JONES. What royalty are you getting on the ore?

Mr. LINDLEY. The royalties vary all the way from 50 to 60 cents for poor grades up to \$1.15 or \$1.20.

Senator JONES. Do you think we could get at any reasonable basis for valuation with such a property as that?

Mr. LINDLEY. They have all been valued in Minnesota. They have a special commission that has been there for a number of years to value mining properties.

Senator JONES. What is it valued at by the Minnesota authorities?

Mr. LINDLEY. They arrive at what they call a present value in the ground, just as the ore lies; and, as I say, using the basis of the Minnesota Tax Commission, the value of all these properties which I have mentioned would be about \$50,000,000.

Senator JONES. And you would be satisfied with that as a basis for invested capital?

Mr. LINDLEY. Yes. All I want is what the property is actually worth.

The CHAIRMAN. When you say what it is actually worth, at what time do you mean?

Mr. LINDLEY. At the time you are levying a tax and allowing a return on the property. I thank the committee.

The CHAIRMAN. The committee will next hear from Mr. John R. Vanderlip. Mr. Vanderlip, we have but very little time this morning. Will you require much time to present your views?

**STATEMENT OF MR. JOHN R. VANDERLIP, OF MINNEAPOLIS,
MINN.**

Mr. VANDERLIP. I should like to take some time.

The CHAIRMAN. That is what I suspected. I wanted to see if you could not limit yourself to some definite time. This is our last day for the hearings, and we are going to be a little pressed for time.

Mr. VANDERLIP. I appreciate that fact, and if the committee will allow me to proceed, when you think my time is up let me know, and then permit me to print my argument and submit it to the committee. With that arrangement I shall be quite content.

Senator McCUMBER. Would it not be well to give us orally now just the points you want to make and submit your argument and have it printed?

Mr. VANDERLIP. Yes; Senator McCumber, I shall be glad to do that.

Senator McCUMBER. I think we should understand it better.

Mr. VANDERLIP. There are two propositions. I represent certain individuals and corporations who are interested chiefly in iron-ore deposits in the Lake Superior region, and from that district, as I am advised, substantially 80 per cent of all the iron ore products of the United States is produced. The two particular points in the proposed revenue bill to which I desire to direct your attention, and for which I desire to ask some modification, are the clause in regard to depletion allowed for natural resources and the definition of invested capital.

Senator THOMAS. Mr. Vanderlip, we have had a number of hearings on those propositions.

Mr. VANDERLIP. Senator Thomas, I think that in respect of the iron markets, especially in the form of a lease, such as is employed in the Lake Superior region, there is a distinction in respect of depletion that does not exist with almost any other mineral.

The particular point in respect of depletion to which I should like to direct attention is this, in the Lake Superior region at least—and I can not speak for other regions—almost all of the iron ore is disposed of under what are called mining leases. By the terms of those leases the lessee agrees to pay a specified price per ton for all the ore that he mines. He is further obligated, whether he mines or not, to pay to the owner of the property an annual minimum sum, being the royalty rate on an agreed number of tons—perhaps a hundred thousand tons. And that is paid whether he mines or not, and after it is paid he is entitled to take out the number of tons of ore for which he has so paid without making any further compensation.

Under the existing law, the act of September 8, 1916, it is provided in general terms—I am not quoting exactly—that the owners of mines shall have the right to deplete to the extent of the value in the mine of the ore which is mined and sold in the taxable year. That does very well where the lessee is mining and taking out his ore. But in those years when he does not mine and take out the ore and pays advance royalties, under the construction that has been put on that law by the Commissioner of Internal Revenue, the owner of the iron property is not permitted to take any depletion and is, on the other hand, required to return all of his royalties received as income and to pay income and excess-profits taxes upon them.

It takes but a moment's consideration to reveal that in those years when the operator takes out ore against the advance royalties that he has already paid in previous years, the mine owner receives no money at all for that ore from which he can make any depletion. That is the general suggestion that I want to make in respect to that, and I desire, therefore, to submit in connection with it a proposed form of a clause for depletion which will protect the iron-mine owners of the Lake Superior district, and, in fact, will protect the owners of all natural resources, whether it be timber, iron, or any other mineral or oils or gas. So much for that.

With respect of the definition of invested capital, I feel, as Mr. Lindley does, that subdivision 2, restricting the value of tangible assets which are paid into a corporation to the par value of the stock issued therefor, works a very great injustice. Prior to 1913, when, for the first time, Congress had authority to levy an income or any other form of tax based upon income, whatever gain there might have been over cost in the value of properties became the capital assets of the owner of those properties, as was distinctly held by the Supreme Court in those recent cases which were decided on the 20th of May and the 3d of June last, and to which I shall take pleasure in referring, if I may print a short brief.

There are to-day thousands of corporations in the United States organized to handle certain properties with practically a nominal capitalization, in return for which properties worth many, many times the par value of the stock were turned in. If this present law be enacted in the form submitted by the Ways and Means Committee, you can see at once the injustice that it will work, and upon that point I think that the definition of invested capital demands some revision.

The same thing occurs in two or three of those subdivisions. I do not want to take up the time of the committee. I have simply out-

lined, as Senator McCumber suggested, the points I desired to make. But if I may be permitted to print my suggestions in regard to both these matters, with a form that I desire to submit to be adopted in lieu of the proposed bill, I shall be very grateful to the committee.

The CHAIRMAN. You can print any amendment you desire, any brief that you have, and any statement of facts that you wish to present.

Senator SMOOT. If you have your brief with you now you can file it with the reporter.

Mr. VANDERLIP. I have only a hurried copy that I dictated, and I shall be glad to print it, if I may.

(The brief referred to above is here printed in full, as follows:)

STATEMENT SUBMITTED TO THE FINANCE COMMITTEE OF THE UNITED STATES SENATE RELATING (A) TO DEDUCTIONS FROM GROSS INCOME FOR DEPLETION OF NATURAL RESOURCES; AND (B) TO THE DEFINITION OF "INVESTED CAPITAL."

I desire to submit for the consideration of the committee some suggestions relating to certain provisions of the new revenue bill particularly affecting taxpayers individual and corporate, engaged in the production and marketing of natural resources, especially iron ore and other essential minerals. The taxpayers whom I represent are interested chiefly in the iron ore deposits of the Lake Superior district, which produces, as I am advised, substantially 80 per cent of the entire iron ore output of the United States. I need not stop to emphasize the vital importance to the Nation in the present crisis of the iron and steel industries, nor the necessity for the uninterrupted production of the raw material demanded for their sustained operation.

What I submit touching the effect of the pending measure upon the iron-ore interests will be equally pertinent, I believe, as respects the owners of other mineral properties, including oil and gas lands, and of standing timber, wherever situated; and I wish to urge modification of some clauses of the bill, as presented to the House by the Ways and Means Committee, which seem to threaten the safety of the interests to which I have referred.

There are certain basic principles which no one, I assume, will question as essential to a fair and equitable tax law, and which it is quite as much to the selfish interest of the Government to observe and conform to as it is to the selfish ends of the taxpayer to have enacted.

For example, it is desirable, from both points of view, that the invested capital of the taxpayer shall be adequately protected from invasion by any exaction alleged and intended to be imposed upon income only. This is so because, if the capital be invaded and reduced by such taxation, there will ultimately be nothing from which income may be produced or derived.

It is of mutual advantage also to both Government and taxpayer that, if excess profits, or war profits, taxes are to be levied upon that portion of corporate gains and incomes which exceeds a certain percentage of the capital invested and used in the taxpayer's business, such percentage shall be calculated upon an accurate, and not upon an arbitrary and inexact, determination of invested capital.

The clauses of the proposed bill to which I direct especial attention are those relating, first, to allowances for depletion of natural resources such as timber, ores, oil, and gas, and, second, to the definition of invested capital.

1. AS RESPECTS DEPLETION.

Paragraph (10) (a) of section 214 (beginning with line 22 of page 15 of the printed bill), relating to individuals, and paragraph (9) (a) of section 234 (beginning with line 20 of page 38 of the printed bill), relating to corporations, provide for the depletion allowances referred to. The two paragraphs are in identical language, as follows:

"(a) In the case of oil and gas wells a reasonable allowance for actual reduction in flow and production to be ascertained not by the flush flow, but by the settled production or regular flow; (b) in the case of mines a reasonable allowance for depletion; (c) in the case of mines, oil and gas wells, a reasonable allowance for depreciation of improvements, such reasonable allowance in all the above cases to be made according to the peculiar conditions in each

case and under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases, the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee."

THE LAW AS NOW EXISTING.

In the act of September 8, 1916 (now in force), Congress disclosed a clear purpose to permit the return to mine owners of the capital investment they had therein on the first of March, 1913. By paragraph 8 of section 5 of that law the same language is used in relation to depletion of oil and gas wells as is found in the pending measure, but, in respect of mines, the language is this:

"In the case of mines a reasonable allowance for depletion thereof not to exceed the market value in the mine of the product thereof which has been mined and sold during the year for which the return and computation are made, such reasonable allowance to be made * * * under rules and regulations to be prescribed by the Secretary of the Treasury: *Provided*, That when the allowance authorized shall equal the capital originally invested, or in case of purchases made prior to March 1, 1913, the fair market value as of that date, no further allowance shall be made."

Please observe that all reference to allowing depletion of natural deposits to an amount equal to the value on March 1, 1913, is omitted in the pending measure, leaving the amount that shall be allowed entirely to the discretion of the commissioner. If the committee can guarantee the continuance in office of the present high-minded commissioner and his equally sincere associates and advisers, this discretionary clause might be permitted to stand; but, in the absence of power to make such guaranty, it would seem the part of wisdom to make the law specific; hence we think this clause should be corrected so as to assure to owners of mining properties the return of their fair values as of March 1, 1913, as a matter of statutory right and not of administrative discretion.

Property rights before March 1, 1913.—It will be borne in mind that until March 1, 1913, Congress had no power to impose a tax upon incomes or profits, and that accordingly that date constitutes a line of demarkation distinguishing the period prior thereto from the ensuing period. Whatever gain or profit a taxpayer derived prior to March 1, 1913, was tax free; he was required to make no account of it so far as the Federal Government was concerned, and so much of it as he did not realize or, if realized, did not spend, became a part of his capital assets; in other words, what he owned on February 28, 1913, was his to the extent of its full value, quite irrespective of how that value accrued, whether by improvement paid for by the owner or by increase of value simply due to lapse of time.

Decisions of the Supreme Court.—This seems sufficiently obvious, but it was put beyond question by the decisions of the Supreme Court of the United States in the cases of *Southern Pacific Ry. Co. v. Lowe*, and *Lynch v. Turrish* (decided June 3, 1918); and in the cases of *Doyle v. Mitchell Bros. Co.*, *United States v. Big Four Ry. Co.*, and *Hays v. Gauley Mt. Coal Co.* (decided May 20, 1918), all recognizing that whatever value existed in the property of a taxpayer at the time the income-tax law became effective constituted a part of that taxpayer's capital assets, including, as the court took pains to emphasize, any increment in value accrued up to that time over the original cost.

It will also be remembered that upon all income, gains, and profits derived by a taxpayer after March 1, 1913, the Government has had and exercised authority to impose income and excess-profits taxes.

Peculiar conditions of mining leases.—It is important to note, however, that the existing law (of Sept. 8, 1916) allows depletion in the case of mines only to the extent of the market value in the mine of ores which are mined and sold during the taxable year. That act fails to reach one phase of iron mining operations and fails to afford protection by allowances for depletion in a situation in which, in a large percentage of instances, the taxpayer receives back before the ore is mined moneys amounting to a substantial part of his capital represented by the value of his ore lands on March 1, 1913.

In the Lake Superior district the common method of disposing of iron ore is by mining contracts, usually in the form of so-called mining leases, under which the contractee or lessee undertakes to pay a specified price per ton for the ore which he mines, and is also obligated, if the mine be not immediately and continuously operated, to pay to the mine owner, in advance of mining the ore, an annual sum representing the agreed price per ton for a definite number of

tons of ore, which sum is received by the owner, and is understood and agreed by both parties to be in full settlement for the ore so paid for, which may be removed by the operator at any time thereafter without further compensation therefor. These payments are commonly designated as "advance minimum royalties"; but whatever their designation they constitute in fact installment payments to the mine owner for the ore in the mine, and to the extent of its value on the 1st of March, 1913, they represent the only payment which the owner receives for such ore and his only mode of recovering his capital invested therein.

Inequitable nature of present law.—The Bureau of Internal Revenue has construed the language of the act of 1916 literally, to wit, as permitting an allowance for depletion of a mining property only to the extent of the ore actually mined and sold during the taxable year; so that in those years where no ore at all is mined and removed, or the amount mined is not sufficient to make up the agreed annual minimum payment, the advance royalties received by the owner are required to be returned as income, and as such are subjected to income and excess-profits taxation; whereas, to the extent of the value on March 1, 1913, of the ore so paid for, these advance royalties represent the return to the owner of his investment. A moment's consideration of the subject reveals that, if the mine owner can take depletion only from payments made for ore actually mined and sold during the taxable year, in those years when the mine operator applies such advance royalties in payment for an equivalent amount of ore mined and removed by him, the owner of the mine receives no moneys from which he can make a depletion deduction on account of the ore so taken out, and, as a consequence, his capital represented by such ore is not received back by him tax free, but is subjected to both income and excess profits taxes. The injustice of this in the past has been great, but, in view of the enormous increase proposed in rates of both normal and excess profits or war profits taxes, it will be multiplied manifold.

AN ILLUSTRATION.

An owner of a tract of land containing 2,000,000 tons of iron ore worth in the mine, on March 1, 1913, \$700,000, or 35 cents per ton, grants a furnace company the exclusive right to mine and remove the ore at a price of 50 cents per ton, showing a gain or profit subject to taxation of 15 cents per ton or \$300,000, in the aggregate.

The lessee agrees to pay \$50,000 per year (the price of 100,000 tons) to apply in payment for that quantity of ore whether it be mined in the same year or later. Of such payment, \$35,000 is invested capital and \$15,000 is taxable gain or profit.

No ore is mined for four years, yet the lessee pays to the mine owner in that period of time an aggregate of \$200,000 (the price of 400,000 tons), upon all of which the owner is compelled to pay income and profits taxes, because no ore is mined and sold during such years, although the actual gain or income subject to such taxation is only 15 cents per ton (or \$60,000), and \$140,000 are a mere return of invested capital.

During each of the succeeding four years the lessee mines and removes 200,000 tons of ore (800,000 tons in all), but pays to the owner in each year only the agreed minimum annual payment of \$50,000, applying the advanced payment of former years in satisfaction of the remainder (\$50,000) of the agreed price. Deducting for depletion the entire sum of \$50,000 in each of the last four years, or \$200,000 in all, the account will stand as follows:

Ore mined, 800,000 tons, value at 35 cents per ton.....	\$280,000
Deduction allowed	200,000

Capital not returned tax free.....	80,000
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If no ore be mined for 10 years, the aggregate minimum payments will be \$500,000, all of which will be taxed as income. If 200,000 tons be mined in each year for the next 10 years, the deposit will be exhausted and the owner will still receive during that period only the agreed minimum payment of \$50,000 per year, or \$500,000 in all. Applying all of this to depletion, the account will show as follows:

Ore mined, 2,000,000 tons, at 35 cents per ton.....	\$700,000
Deduction allowed	500,000

Capital not returned tax free.....	200,000
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If no ore be mined for 15 years, the aggregate minimum payments will be \$750,000, all of which will be taxed as income. If 400,000 tons be mined in each year for the next 5 years, the deposit will be exhausted and the owner will still receive during that period only the agreed minimum of \$50,000 per year, or \$250,000 in all. Applying all of this to depletion, the account will show as follows:

Ore mined, 2,000,000 tons, at 35 cents per ton.....	\$700, 000. 00
Deduction allowed.....	250, 000. 00

Capital not returned tax-free.....	450, 000. 00
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Instances are not infrequent in which mining of ore has been postponed until substantially all the ore in the mines has been paid for in advance, leaving only the annual minimum for one or two years to be paid by the lessor in order to permit the exhaustion of the mine.

Suggested depletion clause.—In lieu, therefore, of paragraph 10 (a) of section 214, and paragraph 9 (a) of section 234, I desire to urge the adoption of a paragraph conforming substantially to the following:

"A reasonable allowance for the depletion of timber, ores, oil, gas, and other natural deposits so as to secure to the taxpayer, whether owner or lessee, a return of the capital invested therein, including cost of development: *Provided*, That if such property were acquired prior to March first, nineteen hundred and thirteen, the fair market value thereof, or of the taxpayer's interest therein, on that date shall be taken to be his invested capital. The amount to be deducted for depletion in any taxable year shall be determined according to the peculiar conditions existing in each case and under rules and regulations to be prescribed by the commissioner with the approval of the Secretary. When the aggregate deductions allowed for depletion in any case equal the total amount to which the taxpayer is entitled as a return of capital, no further deduction for depletion shall be allowed."

II. AS RESPECTS INVESTED CAPITAL.

Invested capital is defined by sections 325 and 326 of the pending bill (at pp. 60 and 61), and I desire briefly to point out some particulars in which the definition in section 326 is inadequate, inequitable, and contrary to business practice.

A definition of invested capital is required in the law for the single purpose of affording a basis for determining the deduction from net income permitted to be made by a taxpayer before the balance of the net income is subject to excess-profits or war-profits taxation. The portion of the income which may be retained by the taxpayer free from this taxation is intended to be such a percentage of the value of the capital used in the business as shall represent a fair return to the taxpayer upon the capital which has earned the income; and no one questions the necessity for such exemption. Manifestly, therefore, it is essential that the amount of that investment shall be accurately and justly ascertained.

1. *Subdivision (1) is unfair to the Government.*—By subdivision (1) of section 326 (a) "actual cash bona fide paid in for stock or shares" is to be reckoned as part of the invested capital.

There is no limitation or qualification of this provision, and, as a consequence, it will embrace, so far as the language of the law is concerned, all of the actual cash at any time paid into the corporation for stock or shares, whether the amount so paid in is still retained in the business or whether it has been, in part or in whole, dissipated through mismanagement, dishonesty, or adverse business conditions. Under the existing law (the act of Oct. 3, 1917) the Commissioner of Internal Revenue has made bold to legislate and to correct this error in a measure by a regulation which requires an accounting for business losses prior to the taxable year; it is desirable, however, that a qualification of the terms of the law should be contained in the law itself, and not be left to extra legislative correction.

2. *Subdivision (2) is in part likewise unfair to the Government.*—Subdivision (2), which relates to the inclusion in invested capital of the actual cash value, at the time of transfer to the corporation, of tangible property other than cash bona fide paid-in-for stock or shares, is open to a similar objection as respects depreciation, exhaustion, or destruction of such property prior to the taxable year.

Both of these clauses, if literally construed and applied, are to the manifest disadvantage of the Government. In fact, in many instances they allow exemptions, in connection with excess-profits or war-profits taxes, based on a larger amount of invested capital than is actually employed in the business.

3. *The same subdivision is injurious to taxpayers.*—As applied to taxpayers I object to the inclusion of the limitation of such value to the time of the transfer of the tangible property to the corporation, for the reason stated in connection with my discussion of the depletion clause, namely, that, irrespective of its cost or its value at the time of acquisition, tangible property owned by a corporation on March 1, 1913, represented invested capital at its then value, the increase being a part of such capital as fully as the original cost to the corporation. This was very clearly declared by the Supreme Court in the cases cited.

Income, profits, or earnings derived from such invested capital after March 1, 1913, are subject to income and excess-profits taxes before what is left can be included as invested capital, so that the limitation to which I have referred is entirely proper as respects property acquired after March 1, 1913, but is erroneous as to property acquired before that date. This is distinctly recognized in section 201 of the bill as the true principle, but that recognition is denied by the language of the bill as it now stands when it comes to its application to excess-profits and war-profits taxes. If injury to the mercantile and industrial enterprises of the country is to be avoided, this distinction must be eliminated from the bill. It is unnecessary for me to assert that few, if any, tax-paying corporations will object to the payment of excess-profits or war-profits taxes at any rates which the situation demands shall be imposed, provided the life of their enterprises is not sapped by such destructive legislation as will forbid their maintenance and development to meet the requirements of business exigencies.

4. *Limitation of value to par of stock issued for property.*—A crying evil in subdivision (2) of the definition is embodied in the words, in line 11 of page 61, "but in no case to exceed the par value of the original stock or shares specifically issued therefor."

There are in the United States to-day thousands of business corporations the capital stock of which was issued in consideration of the transfer to the corporation of tangible property other than cash exceeding in value many times the par of the capital stock issued therefor. Prior to the enactment of the excess-profits tax laws this was a perfectly legitimate transaction of everyday occurrence, instances of which are familiar to all of us. When such corporations were created it was wholly immaterial what the nominal capital of a corporation might be, for it was a fact (and is still an indisputable fact) that the value of the capital stock of a corporation depends upon the value of the assets behind it and has no necessary relation to the nominal par value of the stock. By the clause in the proposed bill which I have last referred to, if a corporation with a moderate capitalization received property in payment therefor of a value several times the par of the stock, all of the value above par will be excluded from consideration as invested capital. It can make no difference in principle whether cash is paid into a corporation and then expended for necessary property, or the property itself is turned in for stock; in either case the eventual assets of the corporation are the same, yet the cash payment is allowed at its full amount, while other tangible property is allowed only at the par value of the stock issued therefor. The injustice of this is apparent and it is not necessary to enlarge upon the subject.

If it is sought to retain the definition of invested capital in anything resembling the form proposed by the pending measure, the words "but in no case to exceed the par value of the original stock or shares specifically issued therefor" should be stricken out of subdivision (2) and a clause substantially as follows should be substituted: "*Provided*, That the actual cash value of such tangible property, clearly and substantially in excess of the par value of the stock or shares issued therefor shall be treated as paid in surplus."

What amounts to an amendment to this effect was in fact appended to the existing law by the regulations promulgated by the commissioner, but, as in the former case of such extralegislative amendment to which I have alluded, it is desirable that the Congress and not the commissioner should embody such amendment in the bill which is finally adopted.

5. *The inhibition against allowing increase of value above cost.*—Subdivision (3) of section 326 (a) relates to paid-in or earned surplus and undivided profits. Surplus and undivided profits earned during the taxable year are properly excluded from inclusion in invested capital, but here again we find the same theory evidenced of excluding from consideration any "increase in the value

of any asset above the original cost until such increase is actually realized by sale."

1. The purpose of this clause seems to be to forestall any attempt by the commissioner to amend the law by regulation, as was done under the act of October 3, 1917. It will be seen that this clause involves the same postulate already adverted to, as, in the last analysis, it applies only to property acquired prior to March 1, 1913. That postulate is, that property belonging to a corporation on March 1, 1913, represented invested capital to the amount of its actual value at that time, irrespective of its cost or value at the time acquired; and this is the postulate which the Supreme Court has declared to be the law of the land.

I have been informed that, according to the calculations of the Treasury Department, not to exceed 10 per cent of all tax-paying corporations will be affected by this clause, but I need not argue that this fact presents no legitimate excuse for its inclusion; on the contrary, inasmuch as it affects so small a proportion of corporations, it seems to me that a desire to prevent any injurious discrimination against them should be a prevailing motive in the drafting of the law, rather than a purpose to select those few for an onerous and excessive burden.

So far as I know, the great majority of the corporations which will be harmed by this proposed legislation are those whose investments are represented, in whole or in part, by lands which are valuable for natural resources therein or thereon, with the single exception that occurs to me of corporations owning business sites acquired long since and which, in the lapse of time, have increased largely in market value. As far as lumbering companies, mining companies, and oil and gas companies are concerned, their lands and developed properties unquestionably represent invested capital essential to the initiation and continuance of their businesses, and such companies are entitled to have the values therein existing on the 1st of March, 1913, computed in arriving at the amount of invested capital on which allowable deduction is calculated, for the reasons already stated.

2. Another very cogent reason against the retention of the clause to which I am objecting is that the proceeds received from the disposition of these wasting properties are almost universally distributed to stockholders as they are received and are rarely, if ever, reinvested in the business of the companies so as to become a part of their working capital. It is a travesty and an aggravation to state to such companies that the increase in value of their properties above the original cost can be included in the calculation of invested capital after such increase is actually realized by sale, when it is certain that after it is so realized it will not be used in the business. From the point of view of a business man, and this tax law is a purely business proposition, the price at which he could dispose of his corporate assets on March 1, 1913, denotes the then value of his invested capital as represented by such assets, and it is submitted that the definition to be embodied in the new revenue law should be one which is in consonance with the recognized understanding and practice of business men the whole country over. A deviation from this principle will produce uncertainty, confusion, and discouragement at a time when stability and assurance are most necessary.

SUGGESTED DEFINITION OF "INVESTED CAPITAL."

6. I desire to submit for the consideration of the committee the following substitute for section 326 (a) as being a fair and adequate definition of invested capital, honest in its operation alike to the Government and to the taxpayer:

"Section 326 (a): That, as used in this title, the term 'invested capital' means: First the actual cash value, as of March first, nineteen hundred and thirteen, of all the tangible property of a corporation used or employed in the business if such property was acquired prior to said date, but exclusive of tangible property the income from which is not subject to the tax imposed by this title; or second, if acquired on or after said date, the tangible property used or employed in the business of a corporation, as follows: (a) cash actually paid in for stock or shares; (b) the actual cash value at the time of payment of tangible property other than cash paid in to the corporation for stock or shares, or, if not paid in for stock or shares, the actual cost thereof in money, or, if otherwise acquired, the actual cash value thereof at the time of such acquisition; third, paid in or carried surplus and undivided profits acquired or ac-

crued on or after March first, nineteen hundred and thirteen, used or employed in the business, exclusive of surplus and undivided profits earned during the taxable year; fourth, also such part of the actual cash value of any inadmissible assets (as defined in section three hundred and twenty-five) as shall be proportionate to the income therefrom which is subject in any taxable year to the tax imposed by this title, to be determined in accordance with regulations prescribed by the commissioner and approved by the Secretary; fifth, where capital stock has been issued in consideration of the transfer to the corporation of intangible property, whether before or after March first, nineteen hundred and thirteen, there shall be included as invested capital an amount not exceeding (a) the actual cash value of such property at the time paid in, or (b) twenty per centum of the par value of the total capital stock of the corporation outstanding on the date of such transfer, whichever is lower."

I appreciate fully the courtesy of the committee in permitting the filing of this statement.

JOHN R. VAN DERLIP.

SEPTEMBER 18, 1918.

The CHAIRMAN. The committee will next hear Mr. F. S. Salmon.

STATEMENT OF MR. F. S. SALMON, NEW YORK.

Mr. SALMON. Mr. Chairman and Senators, Mr. Brown has asked me to speak for a moment in his behalf, and, if possible, to ask that he should be allowed to say a word or two after I have finished. Mr. Brown is here representing the United Real Estate Owners' Association of the city of New York, which consists of some 7,000 members, owners, and lessees of real estate in that city and thereabouts.

One of Mr. Brown's points is identical with that of my immediate predecessor, the gentleman who was taking up the question of the definition of invested capital, on exactly the point of corporations that have turned in tangible property of a value far greater than the par value of the stock issued therefor. In New York City there are a great many corporations that have been formed for holding purposes, for the purpose for sale, and one thing and another, that have turned into the corporations properties greatly in excess of the value for mere nominal issues of stock. I have in mind corporations, for instance, that have turned in properties worth close to a million dollars and have taken in payment therefor stock of a par value of \$5,000. Mr. Brown also has a great many of those corporations in mind.

The law as now passed provides that there is a limit, I believe, to the amount of the par value of the stock issued therefor in the case of corporations who turn in this tangible property prior to January 1, 1914. But the department issued a ruling—article 63—that when tangible property may be included in surplus, where it can be shown to the satisfaction of the Commissioner of Internal Revenue, that excess might be included if paid in surplus. If it is the intention under the present law to continue such a ruling, that would be satisfactory to the real estate interests and the difficulty could be overcome that way. But if it is not, there is going to be a very serious inequity worked along those lines.

The original draft of the law as it was printed in the New York Herald contained a clause in section 2, under the head of "Invested capital," which would have covered that particular subject [reading]:

Unless the actual cash value of such property at the time paid in is shown to the satisfaction of the commissioner to have been clearly and substantially in excess of such par value, in which cases such excess value to be treated as paid-in surplus.

But the draft of the bill as it has been sent out by the Corporation Trust Co., of New York, excludes that particular feature.

Senator SMOOT. It is excluded in the draft.

Mr. SALMON. So that unless this ruling shall be continued as the department has heretofore issued it, I do not see that there would be much relief in a case of that kind.

Mr. Brown's other point is that of borrowed capital, in so far as it affects real estate corporations.

The CHAIRMAN. That ruling you speak of is the ruling made under the present law?

Mr. SALMON. Under the present law—article 63.

The CHAIRMAN. Has the present law been so changed that you think that ruling would not be tenable?

Mr. SALMON. It would seem so, for this reason: I was told that the reason that that regulation was issued was that in the original law as passed there appeared to be a discrimination between corporations organized prior to January 1, 1914, and those organized thereafter, and in order to overcome that discrimination the department issued that regulation. Whether that is the reason or whether only because of the inequity they overcome by that regulation I do not know. Whether they would be under the law entitled to continue such a regulation is beyond my knowledge. I think they might feel they wanted to do it, but I should think rather than put it up to the department to issue a regulation of that kind it would better be in the law itself.

Senator SMOOT. I do not see, with the wording of the House bill, how a ruling could be made such as you suggest here, unless it were a violation of the law in words.

Mr. SALMON. Except they might treat it as they have now, as paid in or earned surplus. If they cared to do it that way, perhaps they might. I do not know. I should think they would have just as much right to do it again as they had in the past. But they have done it. It would appear to me that it would be better to embody it in the law rather than have the question arise, and be determined by the courts afterwards.

Mr. Brown's other point is as to invested capital as it relates to corporations. I have drawn up an example showing how two corporations, both having purchased properties of a million dollars, would fare. The example has been presented to you a number of times. Here are two corporations. One would pay \$5,950 under the excess-profits tax, and the other corporation would pay \$33,600 under the war tax, both in the identical line of business, both owning the same property, with the same income.

I would suggest that you include borrowed money, if it is possible, as capital, inasmuch as such a corporation would have the benefit of an exemption because of the interest paid, that the amount of money annually paid by such corporation as interest should be deducted from the exemption in order to again straighten out the inequity that would occur, and that might be a way of overcoming that difficulty.

Of course, I do not know all the objections to including borrowed money as capital. There might be others. But the capital is there, because we are on the obligation, from the start, in buying the prop-

erty. You have to pay it or your property is taken away, whether you have paid cash or not.

I would like to get this in the form of a brief and mail it to the committee.

The CHAIRMAN. With reference to the briefs, I would suggest that they be in by next Monday.

Mr. SALMON. That can be done in my case. Mr. Browne would like to say a few words, if he may.

The CHAIRMAN. Very well; proceed, Mr. Browne.

STATEMENT OF MR. STUART BROWNE, OF NEW YORK CITY.

Mr. BROWNE. Mr. Chairman, I also represent the real estate board here, at the request of the president of that organization, as well as the United Real Estate Owners' Association.

It has become the custom in New York City, in the last 10 or 15 years, for nearly all pieces of real estate to be transferred to corporations, the principal reason, if not the only reason, being that it is very much easier to handle in the shape of mortgages rather than having individual ownership and subdivisions under which an agreement would have to be made. Whereas now in private ownerships you have the possibility of death of some of the individual owners, rights of dower, and minority children. So that it is almost impossible to handle any piece of property in New York City of any size excepting by means of a corporation. The most of those corporations have nominal capitals, irrespective of value of the property. And most of the capital, of course, is obtained either by individual mortgages or by a fund secured by a deed of trust.

The question of investment capital ought to be looked upon from a different standpoint from that of invested capital in a manufacturing plant or in merchandising. You can, with a manufacturing plant, turn over your capital many, many times in one year, depending upon the number of shifts you are running your machinery and your men. The same thing occurs in merchandising. You will find that businesses can make a gross profit over 100 per cent per annum on their so-called investment, whereas a piece of real estate can only turn over its capital once in a year and sometimes not the whole of its capital once in a year. Therefore I think that in any legislation that is passed mortgage indebtedness or bonded indebtedness on real estate ought to be treated entirely different from borrowed money in other business enterprises such as have been explained already. It ought to be treated as fixed investment, because it is fixed. You can not get it out until you sell the property. It is an absolute impossibility. It is there for good, and sometimes you can not sell the property, you can not even give it away, and therefore borrowed money on mortgages and bonds ought to be looked upon solely as fixed capital.

I think there ought to be an amendment made so as to comply with the regulation that has been made heretofore under the present law as to the surplus, so as to even up the issued capital stock to its real equity. And interest ought to be considered as fixed invested capital, the same as the proceeds of invested capital stock ought to be.

(The following document was submitted by Mr. Salmon:)

NEW YORK, N. Y., September 16, 1918.

HON. FURNIFOLD McL. SIMMONS,

Chairman Senate Finance Committee, Washington, D. C.

DEAR SIR: On behalf of the United Real Estate Owners' Association, which is probably the largest real estate organization in the United States, consisting of some 7,000 members, Stewart Browne, the chairman, desires to present for your consideration the following facts, feeling that some change should be made in the proposed revenue bill to avoid the working of great inequities to the real estate interests, as well as to other commercial enterprises similarly situated throughout the country:

(a) The revenue bill now in force provides that invested capital shall, amongst other things, consist of "the actual cash value of tangible property paid in other than cash, for stock or shares in such corporation or partnership, at the time of such payment (but in case such tangible property was paid in prior to January first, nineteen hundred and fourteen, the actual cash value of such property as of January first, nineteen hundred and fourteen, but in no case to exceed the par value of the original stock or shares specifically issued therefor), and paid in or earned surplus and undivided profits used or employed in the business, exclusive of undivided profits earned during the taxable year."

Many real estate corporations have in the past been formed by various owners, who have taken in payment for their respective interest in the property turned into said corporation the entire stock of such corporation in a sum which is purely nominal, the value of such property being greatly in excess of the par value of such capital stock issued therefore, the purpose of such method usually being for the purpose of admitting of more convenience in case of sale and to better express the interests of all concerned in such property. In accordance with the provisions of the present law, as above set forth, such corporations in determining their invested capital would, so far as such property goes, in the event that such property was paid in prior to January 1, 1914, have been limited to the par value of the original stock or shares specifically issued therefor, but to overcome this inequity a regulation was issued by the Treasury Department as follows:

"ART. 63. When tangible property may be included in surplus: Where it can be shown by evidence satisfactory to the Commissioner of Internal Revenue that tangible property has been conveyed to a corporation or partnership by gift or at a value, accurately ascertainable or definitely known as at the date of conveyance, clearly and substantially in excess of the cash or the par value of the stock or shares paid therefor, then the amount of the excess shall be deemed to be paid in surplus. The adopted value shall not cover mineral deposits or other properties discovered or developed after the date of conveyance, but shall be confined to the value accurately ascertainable or definitely known at that time."

And in accordance with such regulation a company so situated could include in their surplus the value of such property in excess of the par value of the stock or shares paid therefor. The New York Herald in printing a copy of the proposed new bill recently quoted the following provision amongst those covering invested capital:

"(2) Actual cash value of tangible property, other than cash, paid in for stock or shares, at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor, unless the actual cash value of such tangible property at the time paid in is shown to the satisfaction of the Commissioner to have been clearly and substantially in excess of such par value, in which case such excess shall be treated as paid-in surplus."

The bill itself, as finally completed by the Ways and Means Committee, however, in reference to this feature reads as follows:

"(2) Actual cash value of tangible property, other than cash, bona fide paid in for stock or shares, at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor."

It will thus be seen that the paragraph quoted in red above has been omitted from the bill as drawn at present. If it is the intention of the Treasury Department to continue to sustain the regulation contained in Article 63, quoted above, viz: that such excess value may be included as paid in surplus, then no harm will be done because of this omission, but should the Treasury Department decline to continue such ruling, then serious inequity will be worked to the corporations who, when organizing, failed to provide a capital stock of

sufficient amount to represent the actual value of the property turned in, and it is our earnest desire that your committee take steps to see that such inequity be prevented.

(b) We desire further to call your attention to the serious inequity that might be brought about because of the provisions that exclude borrowed capital from being considered as invested capital. In our particular industry, which we have no doubt holds good in a great many other industries, this would cause a penalty to fall upon a corporation engaged in business under identical circumstances with another except that it had to borrow money or assume indebtedness to carry on its enterprise and the other none. For instance, we would cite as an example two real estate corporations, both owning property purchased for \$1,000,000, both with a net income of \$100,000 per annum (figured before corporation (a) deducts the interest on its mortgage, which is at the rate of 5 per cent per annum).

Corporation (a) issued to its stockholders \$100,000, in stock for cash and has bought the property by paying the said sum on account of same and giving or assuming a mortgage indebtedness of \$900,000, at say, 5 per cent per annum.

Corporation (b) has a subscribed capital of \$1,000,000 of its own and has bought the property free and clear, paying the cash therefor.

The following examples would illustrate the war-profits tax that each would have to pay, respectively, under the proposed new bill, and we are assuming for the purpose of simplicity that these companies were not in business during the prewar period:

Corporation (a):

Net income, before deducting interest on mortgage, at the rate of 5 per cent per annum.....	\$100,000
Less 5 per cent on mortgage of \$900,000.....	45,000
Net income.....	55,000
Exemption, 10 per cent on \$100,000.....	\$10,000
Specified exemption.....	3,000
	<hr/>
	13,000

War tax, 80 per cent of..... 42,000=\$33,600

Corporation (b):

Net income.....	100,000
Capital.....	1,000,000
Exemption, 10 per cent on \$1,000,000.....	\$100,000
Specific exemption.....	3,000
	<hr/>
	103,000

The latter corporation could still increase its earnings \$3,000 before it would have to pay any tax of whatsoever nature under the war-profits section. Under the excess-profits method corporation (a) would have no relief; corporation (b) would have to pay as follows:

Corporation (b)—Excess-profits method:

Exemption, 8 per cent on \$1,000,000.....	\$80,000
Specific exemption.....	3,000
	<hr/>
	\$83,000

The balance of the income, amounting to \$17,000, would be subject to tax under the excess-profits method to the extent of 35 per cent thereof, or \$5,950, and it would therefore be clearly shown that these two corporations engaged in the same line of business, both owning the same property, with the same income, in the case of corporation (a) would pay war tax of \$33,600 and corporation (b) a war tax under the excess-profits method of \$5,950. In order to avoid such a serious inequity, we would suggest that, if it is in any way possible, legitimate borrowed money or indebtedness be included as invested capital and to provide that in cases where borrowed money or indebtedness is included in invested capital that as an offset to the benefit that such a corporation would enjoy because of the deduction allowed for interest the amount of interest annually paid by such corporation be deducted from the exemption allowed in such year in computing the war tax under both methods.

We believe both of these points are worthy of your serious consideration and submit the same to you with the hope that it will bring about relief.

Respectfully submitted.

UNITED REAL ESTATE OWNERS' ASSOCIATION.

NEW YORK, N. Y., September 21, 1918.

CHAIRMAN AND MEMBERS SENATE FINANCE COMMITTEE,

Washington, D. C.

GENTLEMEN: The United Real Estate Owners' Association, consisting of over 10,000 members, all residents of and owners of real estate in the city of New York, desires to present, for your earnest consideration, the following facts, and respectfully asks that a change be made in the proposed revenue bill to avoid resulting inequities to the real estate interests as well as to other commercial enterprises similarly situated throughout the United States.

CAPITAL STOCK.

1. The majority in value of parcels of New York City real estate are corporate owned, with very few stockholders and with a capitalization out of all proportion to the equity therein. This condition is brought about by various owners taking in payment for their respective interest in property deeded to the corporation the entire capital stock in the aggregate, generally from 5 to 10 per cent of the equity value in the property.

2. Some of the reasons for New York City corporate ownership rather than partnership coownership are:

(a) Difficulty in forming any agreement which will define the different interests.

(b) Difficulty in getting consent to mortgages and renewals thereof.

(c) Difficulty in getting consent to sale and to facilitate the legal formalities in transfer of property.

(d) To prevent legal complications from deaths occurring and minor interests coming into being as a result thereof.

(e) Preserving continuity in ownership and management, etc.

3. Subsections 2 and 3 of section 207, present revenue bill, read as follows:

"(2) The actual cash value of tangible property paid in other than cash for stock or shares in such corporation or partnership, at the time of such payment (but in case such tangible property was paid in prior to January 1, 1914, the actual cash value of such property as of January 1, 1914, but in no case to exceed the par value of the original stock or shares specifically issued therefor), and."

"(3) Paid in or earned surplus and undivided profits used or employed in the business, exclusive of undivided profits earned during the taxable year."

Under the above law the capital of such corporations, for the purpose of the war tax, would be limited to the par value of their capital stock provided the property was transferred to the corporation prior to January 1, 1914. The inequity of this was clearly seen by the Treasury Department, and they therefore issued the following Treasury Regulation:

"ART. 63. When tangible property may be included in surplus: Where it can be shown by evidence satisfactory to the Commissioner of Internal Revenue that tangible property has been conveyed to a corporation or partnership by gift or at a value, accurately ascertainable or definitely known as at the date of conveyance, clearly and substantially in excess of the cash or the par value of the stock or shares paid therefor, then the amount of the excess shall be deemed to be paid in surplus. The adopted value shall not cover mineral deposits or other properties discovered or developed after the date of conveyance, but shall be confined to the value accurately ascertainable or definitely known at that time."

Section 326, subdivision 2, of the proposed new bill as drafted originally by the Ways and Means Committee reads as follows:

"Actual cash value of tangible property, other than cash, paid in for stock or shares, at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor, *unless the actual cash value of such tangible property at the time paid in is shown to the satisfaction of the commissioner to have been clearly and substantially in excess of such par value, in which case such excess shall be treated as paid-in surplus.*"

The bill itself as finally drafted by the Ways and Means Committee, for presentation to the House, eliminated the above matter in italics and instead of said section, section 326, subdivision 2, was inserted, reading as follows:

"Actual cash value of tangible property, other than cash, bona fide paid in for stock or shares, at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor."

We are legally advised that the wording of the proposed new bill will completely wipe out said article 63 of the Treasury Regulations. The following

will give you a glaring illustration of the inequity arising out of the bill as now drafted, on a property valued at \$1,000,000, with a mortgage of \$700,000, with the owning corporation capitalized at \$10,000 or capitalized at \$30,000:

(A) Corporation—\$10,000 capital stock:	
Net income—without deduction of interest.....	\$70,000
Interest.....	35,000
Net income.....	35,000
Specific exemption.....	3,000
	32,000
War tax of 35 per cent of \$32,000.....	\$11,200
(B) Corporation—\$300,000 capital stock:	
Net income—without deduction of interest.....	\$70,000
Interest.....	35,000
	35,000
Exemption 10 per cent on capital of \$300,000.....	\$30,000
Specific exemption.....	3,000
	33,000
	2,000
War tax of 80 per cent on \$2,000.....	1,600

Showing that corporation (B) will pay \$9,600 of war tax more than corporation (A) with the same property and the same net income, but only a difference in the capital stock. To meet this condition we respectfully ask that the above section be amended to read as originally drawn by the Ways and Means Committee, as outlined above, by adding to section 326 the paragraph—

"Unless the actual cash value of such tangible property at the time paid in is shown to the satisfaction of the commissioner to have been clearly and substantially in excess of such par value, in which case such excess shall be treated as paid-in surplus."

INTEREST ON MORTGAGE INDEBTEDNESS.

4. Fully 90 per cent of the fixed capital invested in New York City business and apartment property is furnished by mortgage indebtedness, while 70 per cent of the property in Boston is represented by shareholders' investment to 100 per cent of its value and without mortgage indebtedness. The inequity of the war tax on New York City real estate as compared with Boston real estate and other real estate similarly situated can be readily seen.

There are thousands of properties where the proposed war tax would take practically all the net profits (except the \$3,000 specific exemption) and where such exemption represents an infinitesimal percentage on the equity value. The following is but one illustration of the inequity of the proposed new bill, assuming for the purpose of simplicity that these corporations were not in business during the prewar period and each owning the identical property of a value of \$1,000,000:

(A) Corporation—\$100,000 capital stock:	
Net income without deduction of interest.....	\$70,000
5 per cent interest on mortgage of \$900,000.....	45,000
Net income.....	25,000
Exemption 10 per cent on \$100,000 capital.....	\$10,000
Specific exemption.....	3,000
	13,000
War tax of 80 per cent of \$12,000.....	\$9,600
Net income.....	2,400
Equal to 2.4 per cent on its \$100,000 equity.	
(B) Corporation—\$1,000,000 capital stock:	
Net income.....	70,000
Exemption 10 per cent on \$1,000,000 capital.....	\$100,000
Specific exemption.....	3,000
	103,000

Corporation (A) would pay a war tax of \$9,600, whereas corporation (B) would pay no war tax whatsoever under either the war-profits method or excess-profits method.

To remedy the above or similar inequities, we respectfully suggest that mortgage indebtedness on real estate be included as invested capital, and to offset the advantage that any corporation with a full mortgage indebtedness would have over another corporation with a lesser or no mortgage indebtedness the interest paid on mortgages annually by any corporation should be deducted from the exemption allowed in such year in computing the war-profits method or excess-profits method.

CONCLUSION.

The bill as now drafted has the following inconsistencies, of which only four examples have been given, as above.

A corporation owning realty of the same value, same income, some mortgage indebtedness will pay a war-profits tax or an excess-profits tax varying in amount from nothing to nearly 80 per cent of net income, depending upon the corporation's capital stock amount.

A corporation owning realty of the same value, same income, same capital stock amount will pay a war-profits tax or an excess-profits tax varying in amount from nothing to nearly 80 per cent of the net income, depending upon the amount of mortgage indebtedness.

The bill as drafted puts a premium on overcapitalization and upon wealth, and penalizes undercapitalization and poverty.

The whole of the above is respectfully submitted to your committee for your careful and earnest consideration and in the hope that it will bring real estate relief.

UNITED REAL ESTATE OWNERS ASSOCIATION,
By STEWART BROWNE, *Chairman*.

The above brief is hereby indorsed.

REAL ESTATE BOARD OF NEW YORK,
By LAURENCE MCGUIRE, *President*.

The above brief is hereby indorsed.

ADVISORY COUNCIL OF REAL ESTATE INTERESTS,
By WALTER LINDNER, *Chairman*.

MOTION-PICTURE INDUSTRY.

On behalf of the motion-picture industry there appeared a delegation consisting of Mr. William A. Brady, president of the National Association of the Motion Pictures Industry; Mr. Walter V. Irwin, general manager of the Vitagraph Co.; Mr. Frederick H. Elliott, and others.

The CHAIRMAN. Mr. Elliott, of New York, has asked for a hearing.

Mr. ELLIOTT. Mr. Chairman, Mr. Brady is here, and will address the committee.

STATEMENT OF MR. WILLIAM A. BRADY, PRESIDENT OF THE NATIONAL ASSOCIATION OF THE MOTION PICTURE INDUSTRY.

The CHAIRMAN. Mr. Brady, you represent the same interests Mr. Elliott represents?

Mr. BRADY. Yes, sir. I am the president of the National Association of the Motion Picture Industry. I represent the motion-picture industry, the making of the pictures, the distributing of the pictures, the exhibiting of the pictures, and everything connected with the industry.

Senator SMOOT. As well as the very charming young lady who plays?

Mr. BRADY. I thank you very much.

We do not come here at all as squealers. I dare say that when the history of this war comes to be written, the most marvelous achievement and the most marvelous development of any industry in the world will be the development of the uses of the motion picture to win this war.

On the 28th of June, 1917, our worthy President wrote these lines:

It is in my mind not only to bring the motion-picture industry into fullest and most effective contact with the Nation's needs, but to give some measure of official recognition to an increasingly important factor in the development of our national life. The film has come to rank as a very high medium for the dissemination of public intelligence, and since it speaks a universal language it lends itself importantly to the presentation of America's plans and purposes.

May I ask you as chairman by my appointment, to organize the motion-picture industry in such manner as to establish direct and authoritative co-operation with the Committee on Public Information, of which Mr. George Creel is chairman?

That letter was directed to my humble self. And during the last 18 months I think it is a well known fact to you all that the motion picture has delivered worthy and valuable service to the Government. It has not charged for its services, it has not come here asking for reductions or concessions or favors of any kind. It has come to all the departments in the city of Washington, and it has offered its services gratis.

In the next Liberty Loan it is dedicating, free of cost, to the Treasury Department at least 45 pictures made by the men and women of the screen at their own expense, developed, printed, lighted, and produced by the manufacturers and the producers of the United States, and, in the opinion of the Secretary of the Treasury, those pictures are going to be a most valuable propaganda that is to be used in the coming Liberty Loan. Let that suffice for what we have done, and alibi us to the extent that we do not come here trying to squeal.

We think that the taxes that are to be put upon us will practically drive at least 50 per cent of the theaters of the United States out of business.

Senator THOMAS. Mr. Brady, you exported 160,000,000 feet of film in 1917, did you not?

Mr. BRADY. Yes, sir.

Senator THOMAS. That was either on sale or lease?

Mr. BRADY. In some cases on sale and in some cases on lease.

Senator THOMAS. One or the other?

Mr. BRADY. One or the other.

Senator THOMAS. What are your terms of sale and what are your terms of lease?

Mr. BRADY. They vary.

Senator THOMAS. Give us the average.

Mr. BRADY. An ordinary picture in Great Britain will sell for \$4,000 to \$5,000. An extraordinary picture might sell for \$50,000.

Senator THOMAS. What is your average per foot?

Mr. BRADY. I should say from \$4,000 to \$5,000.

Senator THOMAS. \$4,000 to \$5,000 per foot?

Mr. BRADY. Outright sale.

Senator THOMAS. You sell and lease by the foot, do you not?

Mr. BRADY. Not in the foreign countries. The practice in some foreign countries is to buy outright at so much per foot and so much for the picture in other countries.

Senator THOMAS. What was your total revenue for that 160,000,000 feet of film sold and leased last year?

Mr. BRADY. I will ask Mr. Irwin to answer that.

Mr. IRWIN. For the United States and Canada the total film rentals are \$70,000,000 a year.

Senator THOMAS. That excludes your exports to France, to England, and to other places?

Mr. IRWIN. Yes, sir.

Senator THOMAS. The 160,000,000 feet constitutes your total exports, does it not?

Mr. IRWIN. At the present time, Senator, we are using about 400,000,000 feet of positive film.

Senator THOMAS. That is not export. I am talking about the export of last year of 160,000,000 feet.

Mr. IRWIN. Our export would not average over 8 cents a foot.

Senator THOMAS. Eight cents a foot?

Mr. IRWIN. Yes, sir.

Senator THOMAS. That would be a little over \$12,000,000 for 160,000,000 feet. You do not pay a cent of tax on that, do you?

Mr. IRWIN. Yes.

Senator THOMAS. I am talking about your sales and your leases.

Mr. IRWIN. No; not on the sales or leases. But we do pay upon the goods which we purchase with which to make the pictures.

Mr. BRADY. But, with all that, Senator, no film company in this country has declared any dividends during the last year. The film industry has not profited by the war. We have rolled up no great surplus. What surplus we may have is in film, lying on shelves. We claim you are taxing us more than you are any other industry in the United States.

Senator THOMAS. A great many people who appear before us claim that.

Mr. BRADY. The figures can not lie.

Senator THOMAS. That is what we have been told by representatives of other industries.

Mr. BRADY. You are taxing us 20 per cent on every admission to our theaters, and, beyond that, you propose to tax us 10 per cent on every film rental.

Senator THOMAS. You pass your 20 per cent on to the fellow who buys the ticket, do you not?

Mr. BRADY. Yes, my dear Senator; but at the same time it will decrease our business. A 10 per cent tax we did not complain of when it was imposed, but that 10 per cent tax did this: There were 17,000 motion-picture theaters in the United States when that tax went on. There are less than 14,000 now.

Senator THOMAS. You have raised your prices, possibly.

Mr. BRADY. In very few instances.

Senator THOMAS. Is that strictly correct, now?

Mr. BRADY. I am informed that the other day a gentleman representing the vaudeville interests of the United States was asked

whether he had not increased his prices at Keith's Theater. You must not take Washington as a gauge of the amusement business of the United States. Washington at the present time is the most prosperous place in the United States.

Senator THOMAS. No; I should not say so. I bought some tickets at a stand in New York, and I judge to some extent by that.

Mr. BRADY. If you talk about New York, then I want to call your attention to a very marvelous clause you have in this bill. I can quote it without looking at it. The stands in New York are charging 50 cents premium. It is the custom in New York for that to be divided between the theater owner and the stand, as you call it. You tax the theater owner 50 per cent of his 25 cents and you tax the stand owner 5 per cent of his 25 cents. The stand has no investment; the stand sells the seats. Last week they sold seats for a very popular patriotic play, "Yip, Yip, Yaphank," for as high as \$5 a seat. It came to the notice of the district attorney in New York. Therefore it is not right that you should hold us up for that sort of thing.

Senator THOMAS. I am not doing that.

I may say, in that connection, that in the consideration of the bill of 1917 I exerted every effort I was capable of in taxing that very situation; but it disappeared from the bill in conference.

Mr. BRADY. Yes; very strangely disappeared, Senator.

Senator THOMAS. I would not say that. It disappeared.

Mr. BRADY. It has disappeared.

The CHAIRMAN. I do not think that sort of remark is justified—"strangely disappeared." It is a reflection on the conferees.

Mr. BRADY. I did not intend it that way at all. I might also call attention to the fact that you were kind enough in this committee to eliminate the footage tax, and the footage tax appeared back in the bill finally.

But to come down to what I appear for, I plead as perhaps the oldest theatrical man in the United States actively engaged. I must be an expert; you consult with representatives of other industries of the United States as to what you are going to do with them; you consult with experts on steel, rubber, leather, or any other commodity. I say that in this instance at least you should take into consideration the expert judgment of a man who has passed his whole life in the entertainment business, and I say to you that just as surely as we are in this room this estimate made here will not be justified by the event. It is estimated that from admissions for the fiscal year 1918 there were \$26,357,000; for the fiscal year 1919, under existing law, estimated \$50,000,000; and for the 12 months' period under the proposed bill, \$100,000,000. I desire to go on record as an expert as saying that that estimate in the last column will not come true, and that it is very likely the estimate of the second column will decrease with the increased taxation. I put it up to any gentleman here that if he goes to the box office of the theater and is called upon to pay 10, 15, 30, 40, or 50 cents over and above the already pretty stiff prices that they charge in some theaters, that he will think it is becoming hard. It is my business to sit in the box office and watch the public and get the pulse, and I can see it coming now, even in anticipation of this tax. The business is decreasing all over the country; not in

Washington, true; not in New York, true; not in Chicago, true; and not in Boston, true. But they are not the United States.

Senator THOMAS. Have you among your stars a young woman named Anita Roberts or Anita Williams?

Mr. BRADY. Anita Stewart.

Senator THOMAS. Is it a fact that you pay her \$3,500 a week?

Mr. BRADY. I am not quite positive of it, but I think so. And I might say that if that young lady gets that amount of money, she will have to give about 60 per cent of it to the Government.

Senator THOMAS. I hope so.

Mr. BRADY. If it is true, and it is stated. In meetings between theatrical interests and the governing bodies of the United States three names always come up—Charlie Chaplin, Mary Pickford, and Douglas Fairbanks. Let us say that those people are getting very large salaries, which they earn, because their pictures sell the world over. Those names I have just mentioned sell as well in India as they sell here. Is it not a fact that if Mary Pickford makes \$500,000 or \$700,000 or \$1,000,000 a year, the Government is going to take 60 per cent of it?

Senator THOMAS. But it strikes me that a business that can pay salaries like that, even in war times, is doing pretty well.

Mr. BRADY. The fact nevertheless remains that we have declared no dividends. These actors are getting the money.

Senator THOMAS. There are lots of industries we are taxing that have not declared any dividends, and are not likely to, during war times.

Senator JONES. I was just going to ask you about that. How much has your inventory increased during the last year?

Mr. IRWIN. Our inventory has not increased, and our inventory is really fictitious.

Senator JONES. That probably is the reason it has not increased.

Mr. IRWIN. No; in this respect, Senator: It was necessary for us, in order to show any profits at all upon which to borrow money, in some cases to pay our tax, to inventory our negatives upon their former value, the value when we were able to sell those negatives abroad. At the present time our foreign business is very greatly decreased. Yet our balance sheet shows our negatives put in at their former value. The net result is that previously we used to receive, on a class of picture that cost \$26,000, a gross profit of \$54,000 from the United States and our European sales. Where our European sales are cut off we receive a gross profit of only \$19,000. Yet we have had to value those negatives and have taken them up at their former value. The net result is that there has been a tremendous accumulation of negatives that we hope to dispose of abroad. But the chances are that when the war is over the European market will never be able to digest the tremendous supply that is now on the shelves ready to be sent abroad, and has been accumulating for four years. I have the actual figures here on that. A certain class of negatives costs on the average \$26,000. Fifty prints for use in the United States cost \$10,000, making the total cost \$36,000. When fully used abroad, add 30 prints costing \$6,000. Cost if used only in the United States, \$36,000. Cost if used abroad also, \$42,000.

Senator JONES. Do you mean to say that you have been making those great expenditures in piling up goods on the shelves, as you call

it, when you feel that you are never going to get your money out of them?

Mr. IRWIN. Yes, sir.

Senator JONES. Why do you do it?

Mr. IRWIN. We have been making those expenditures. Our negatives are costing us more to-day than ever before.

Senator JONES. If you have no use for the negatives, can not get any money out of them, why do you put money into them?

Mr. IRWIN. We are endeavoring to get as much money as possible from them in the United States and Canada, and we are hoping to get our usual profits from them abroad; but the chances are we will never be able to accomplish that end.

Senator JONES. As a business man, do you mean to tell me that you are putting your money into those things when you honestly believe the chances are you will never get your money out?

Mr. IRWIN. Yes, sir; and, Senator, I will tell you why. The competition in this business is so keen that the company that does not continue its expenditures, and continue a product that is in advance of the public demand, soon falls to the wayside. No company in this industry can stand still. Our product must always be in advance of the public demand. There are millions and millions of people coming to the motion-picture industry as patrons who never saw a motion picture a year ago or two years ago. Had we talked to you gentlemen of motion pictures two years ago the chances are that most of you would not have ever seen a motion picture. Yet to-day you are well acquainted with them. There are millions and millions of people coming to the screen every day as patrons. Our product, in order to hold those patrons, must be in advance of the public demand as to merit, as to artistry, as to acting, as to production, as to setting, as to stories, and with the cost of everything increasing, the competition among ourselves is so great that no company can let up. One manufacturer was asked in a meeting with the exhibitors, "If you are losing money, why do you continue in business?" This president of one of the largest manufacturing companies answered, "We will continue in business just as long as we have 5 cents to take the subway and go down to Wall Street."

Senator JONES. If you gentlemen had recently escaped from St. Elizabeths I would not wonder at your argument. But I never saw two gentlemen appear before the committee who looked as if they had more good, bright business sense and judgment than you two gentlemen, and to have it appear in this record that you are contending that you are deliberately investing money in a thing which you deliberately believe you will never get it out of is beyond the comprehension of at least one member of the committee.

Mr. IRWIN. Senator, we must do so or quit. May I point this out to you? If you will look at our balance sheet you will see the tremendous amount of money we owe to the banks, and you will see that in many instances we have borrowed that money.

Senator JONES. And still are borrowing the money to put it into a thing from which you never expect to get it out?

Mr. IRWIN. We do hope to get it out when this war is over, but the chances are growing less as the war continues. We have hoped that when we made a negative that was very expensive we would get our

usual profit from that negative. But as the war goes on from year to year we are becoming more fearful that the congestion of product will prevent it.

Senator THOMAS. You spoke of competition. I understood Mr. Brady to say, when he began his discussion of this matter, that he represented the entire industry of the United States.

Mr. IRWIN. He does.

Senator THOMAS. Then you are combined for the purpose of resisting this tax?

Mr. IRWIN. No, Senator; we are only combined in an association for the protection and the promotion of our own welfare, and since this country entered the war that association has devoted itself to no other work than the promotion of the war.

Senator THOMAS. But they are cutting each other's throats by investing in ways that you say will probably never realize a profit?

Mr. IRWIN. Unfortunately, we are. Unfortunately, we may have an artist under contract to-day—to cite an unfortunate condition of a young industry—and an opposition producing company will come and make an offer to that artist, even though the artist is under contract, which will make that artist so unhappy and sulk to such an extent in the work that we have to amend the contract and increase the weekly compensation. Those are evils in the industry which will only be corrected through such an association.

May I just point this out to you, that if you will look at our income sheets you will see that the producing and distributing branch of the industry last year did not earn \$5,000,000. This is a tax of 10 per cent on our gross rentals. Our gross rentals are \$70,000,000. The tax will be \$7,000,000, at least \$2,000,000 more than we are earning. Not a company, Senator—although it may appeal to you as very bad business, and doubtless there are many bad business executions in this industry, which will correct themselves as the industry grows older—paid a dividend last year.

Senator TOWNSEND. I understood Mr. Brady said you did not object to the 10 per cent tax.

Mr. BRADY. We do not object to the 10 per cent tax in the present law on admissions. It is the intention in the next law to raise it to 20 per cent and to ask, further, a 10 per cent tax on rentals.

I will ask you now to listen to an exhibitor, a man from Maine, who represents the men who run the theaters, Mr. Alfred S. Black.

The CHAIRMAN. You may proceed, Mr. Black.

STATEMENT OF MR. ALFRED S. BLACK, OF MAINE.

Mr. BLACK. Mr. Chairman, I represent the exhibitors' branch of the motion-picture industry, representing the theaters of the United States. This is the first time that the small theater has come to Washington to be heard. I will try to be very brief and confine my remarks to business statements.

The exhibitors are a unit to win the war, and, as Mr. Brady has stated, without thought of profit. We are willing to pay a just and fair tax—glad to do so—but ask you not to make the tax so burdensome as to put a large number, especially of the small theaters, out of existence. Mr. Brady has shown you what the theater has done in the

conduct of the war. I shall not touch upon it, but simply want to emphasize the fact that it is one of the biggest assets to the Government, and I hope you will take that thought away with you when you leave this committee room.

There are three different taxes:

First, the seating tax, which the proposed bill increases to a double amount, exempting the small theater in towns and cities of 5,000. If this was the only tax to be increased, the exhibitor would not object.

The second tax is the change, or proposed change, from the footage tax to the 10 per cent on rentals. It is estimated that the present footage tax pays the Government approximately \$2,300,000, and that the new proposed tax will amount to approximately \$7,000,000. The manufacturers have ably stated that they can not afford to pay this tax, which is true. But it is even more true that the exhibitor can not afford to pay the tax, and there is no way that he can pass this tax over to the public unless by means of profiteering through increased admissions, which causes a very material falling off in his business.

The third tax is the increase of the admission tax from 10 to 20 per cent, which is the most dangerous of all. When the 1917 tax was put in force, it is an actual fact that there was a falling off in business of at least 25 or 30 per cent. It was four or five months before anything like normal conditions came back, and they have never recovered, especially with the small theater.

The small theater comprises approximately 75 to 80 per cent of the total theaters in this country, and to-day they are laboring under a great burden. The tax not only closed, as estimated, some three to four thousand theaters, but the gradual draft—with the exception of a very few towns which are being benefited by war activities, and they are in the minimum—is weakening the existence of the exhibitors, so that these few theaters which have been able to show a small profit are now going into the loss column and can not stand further taxation and remain open.

We feel that if this increased admission tax is put into effect it will be more effective in cutting out theater attendance than the 1917 tax was, and that the Government will get a very small proportion of the increased taxes estimated, and they will be losing the effect of the screen, which has been so important to the causes of the war. We ask you to consider the exhibitor, and especially the small exhibitor; that we have a double taxation at the present time, a seating tax, and, in addition to that, we pay numerous State, county, and city taxes, and various licenses, and a censorship tax. Those are all burdens upon the exhibitor which can not be passed over to the public. But there is really a double taxation, with a seating tax and a so-called footage tax, or a proposed percentage tax. It is more in proportion than any other industry pays in that we can not turn it over; and then, on top of this, the grave danger of increasing the tax so that it will drive away the patrons from the theater, which is an all-important thing at the present time. It means more to the Government, in our judgment, to have the people attend the theaters where they can get the propaganda that is so necessary for them to receive at the present time, where they can gather together for the successful outcome of these various drives, and so on, as Mr. Brady has ably referred to, than it is to get the additional amount that might

be obtained by the Government in this additional tax, and I urge you, as strongly as I can, from the exhibitors of the United States, to consider that and not put a burden upon them that will eventually drive out of business a very large percentage of the exhibitors of this country.

Mr. BRADY. Senator, may I say one more word to correct something that was said, so that it may go into the record?

The CHAIRMAN. Yes.

Mr. BRADY. Senator Thomas, you said we were combined to fight this tax?

Senator THOMAS. You said you represented everybody.

Mr. BRADY. The only reason why I represent everybody here is because the only way they could all be brought into one concrete mass was through the letter of the President. They are all in one concrete mass, with many divided interests, with the interest of the exhibitor who has just spoken entirely different from Mr. Irwin's interest. But for public service only are they in a concrete mass, not for fighting any taxation.

Senator ROBINSON. They could not have all been heard. They necessarily had to have some one to speak for them.

Mr. BRADY. That is true.

Senator ROBINSON. We could not have heard every diverse interest among them.

Mr. BRADY. That is true.

The CHAIRMAN. We asked that the industries, as far as practicable, select some one to speak for them, and I think you are just simply complying with the request of the committee when you come as the representative of the whole industry.

Mr. BRADY. That is right.

The CHAIRMAN. You said something in your statement a little while ago that might have been interpreted to mean that you did not think your industry was getting as full and fair a hearing before this committee as other industries did.

Mr. BRADY. I feel, Senator, that the other industries are very well known. You know all about iron ore; you know all about newspapers; and you know all the other great industries. But this industry is a young industry, and you may not understand about it. For instance, you take the Senator's argument as to what a fool a man must be to go on making expenditures each week and no profit coming in.

Senator THOMAS. That was not it. What Senator Jones criticized was the statement that you were making these investments with no expectation of getting a return, but expected to lose them.

Mr. BRADY. Let me give you a concrete illustration of what the Senator referred to. I was the head of the World Film Co. for two years, and I received a very large salary as an expert producer. That company went on for two years while I was the managing director of it, and it was forced to produce a picture every week for this reason, that the motion-picture houses throughout the United States must have an issue each week. Pictures, as a general rule, run only one night. That company invested in the two years an average of from \$25,000 to \$30,000 weekly in a five-reel picture, and yet at the end of the two years, with all that stuff on the shelf, as

you say, their bank roll had decreased 500 per cent, and still they had to go on, hoping and hoping and hoping, and producing, and hoping that some day, as in the case of the General Motors Co., they would be able to make some money. I think that is the best illustration I can give you. You remember when the automobile was a luxury, when there was a great break in Michigan, and an automobile man's note was not worth 30 cents, and there were all kinds of men manufacturing automobiles and getting a bit here and a bit there and a bit there, and all sorts of people running in the automobile business. Then suddenly there came a great crash; the automobile business went flat on its back, and then some smart men stepped in and picked out the responsible units of that business and made the entire car themselves—went at the business in a businesslike way—and the automobile business became a great proposition.

I assert this, that the great man is some day going to come to the film industry. The film industry at present should be far beyond where it is. It should not be entertainment. The day is going to come when children are going to be taught by film. Instead of making education irksome for the child, you are going to make education pleasant for the child. The bird, the snake, the caterpillar turning into the butterfly, will be shown to the child on the screen, so that he or she will enjoy it. The operations of great physicians on the eye and the ear will be taken for the screen, and a close-up will be exhibited for years and years to students in the colleges of this country. Therefore, when that great man does come, he will lead this industry out of the wilderness, the same as other great man led the automobile business out.

The CHAIRMAN. What I had in mind to say was that, so far as the film industry is concerned, this committee has given every person who has come in asking to be heard in behalf of that industry a full and ample opportunity.

Mr. BRADY. You were kindness itself to us a year ago.

The CHAIRMAN. And I want to say further that in the conference of the two Houses on the last bill I do not think any subject occupied the time of that conference longer than the question of the tax to be imposed upon the film industry. You had some very strong champions upon that conference committee. I remember very well the very eloquent speech which you made to the committee in behalf of your industry at that time. I am glad you came back and have given us your views with reference to this bill, as you did with reference to that.

Mr. BRADY. You must always remember it is the poor man's entertainment, and it is keeping many a man from a worse place.

Mr. IRWIN. May I say to Senator Jones, in answer to his criticism, that it is necessary for us to continue to make pictures for the United States that cost just as much and more than the pictures which were formerly used for the United States and abroad. The fact that our market is restricted abroad can not relieve us from making the same high-class pictures for the United States, and hoping that we will some day get our money out of the foreign market.

Senator JONES. What I was criticising was the fact that you did not hope to get it back and did not expect to get it back.

Mr. IRWIN. We have to continue to make the pictures for the

United States or go out of business, and we can not decrease the merit of the pictures we may offer. So that we either have to continue to make pictures for the United States or go out of business, and that is the problem that confronts the business.

Senator JONES. You have to continue to make these pictures and pile them on the shelves for foreign use that you do not hope to make?

Mr. IRWIN. Yes, sir; because we make them for the United States. You see, the same negative that is made for the United States is made for the world. The foreign market merely consists of taking additional positives. We can make as many positives from a negative as we want, a thousand or 10,000. Our foreign market consisted simply of making 30 more positives and shipping them to the foreign markets. That has been restricted. Our great cost is in our negative. Our negative costs us probably \$25,000 or \$30,000. Our positives cost us probably \$250 apiece. We never make a negative for the foreign market. We make our negative for the world, and where we have lost our revenue has been cut off from the positives we shipped abroad.

Mr. BLACK. Mr. Chairman, I wanted to bring up just this one point, that in the production of pictures the stars' salaries play a very large part. The star pays a tax on his salary, and when the proposed percentage on the cost of production is made it makes really double taxation. I simply wanted to bring that point clearly before you.

(A memorandum prepared by the National Association of Motion Picture Industry was submitted, and is here printed in full, as follows:)

[Memorandum prepared by a committee of the National Association of the Motion Picture Industry in respect to the film-footage tax of the revenue act of Oct. 3, 1917. Arthur S. Friend, chairman; William A. Brady, president; ex-officio members, Walter W. Irwin, David P. Howells, Lee A. Ochs, H. B. Varner.]

The film-footage tax as enacted and now in effect, is unique in that in effect it is a penalty levied upon persons, firms, and corporations engaged in a business which, instead of being of the type ordinarily penalized or licensed, is in fact, one which benefits the Government, and whose uses and purposes are directly employed by the Government. In other words, we find the legislative department of the Government in effect, condemning what the administrative department uses, encourages, and seeks to maintain.

It would seem that this tax developed out of a complete misapprehension of the nature of the motion-picture industry, because it is inconceivable that Congress should have deliberately attempted to cripple an industry in respect to which the administrative department of the Government has repeatedly and positively spoken. The President, at the very beginning of the war, put himself clearly on record. Every word contained in his letter of June 28, 1917, addressed to Mr. William A. Brady, president of the National Association of the Motion Picture Industry, is worthy of consideration, and, accordingly, the letter is here set forth in extenso:

THE WHITE HOUSE,
Washington, June 28, 1918.

MY DEAR MR. BRADY: It is in my mind not only to bring the motion-picture industry into fullest and most effective contact with the Nation's needs, but to give some measure of official recognition to an increasingly important factor in the development of our national life. The film has come to rank as a very high medium for the dissemination of public intelligence, and since it speaks a universal language it lends itself importantly to the presentation of America's plans and purposes.

May I ask you as chairman by my appointment, to organize the motion-picture industry in such manner as to establish direct and authoritative cooperation

with the Committee on Public Information, of which Mr. George Creel is chairman?

It is much to ask, but my knowledge of the patriotic service already rendered by you and your associates makes me count upon your generous acceptance,

Cordially and sincerely, yours,

WOODBROW WILSON.

MR. WILLIAM A. BRADY,

157 West Forty-eighth Street, New York City.

That the administration's appreciation has not diminished, but has, in fact, increased, is best shown by the acts of the several department heads, although of course, verbal expressions are not lacking. Substantially all of the administrative departments of the Government—notably the Treasury Department, the War Department, the Navy Department, the Department of Agriculture, the Food Administration, the Fuel Administration, and the Department of Training Camp Activities—are using the motion pictures as an integral part of their work, and in many instances have established and are maintaining completely organized motion-picture branches in their departments. The Red Cross also uses the motion picture, and most successfully. And it is to be noted that not alone is recognition given to the fact that the motion picture is "a very high medium for the dissemination of public intelligence," but also is recognition given to the fact that the motion picture provides entertainment and relief which is essential in the strenuous and critical times in which we now are. That America will win her war is beyond doubt, but just as it is important that the money, the ships, the food that are essential must be provided that the men who fight may fight well, so, too, is it essential that the psychology of the men at the front and the men and women at home be recognized and be protected. In every cantonment in America motion pictures are provided for the entertainment of the soldiers, and in every camp in France motion pictures are provided for the soldiers; in every naval training school motion pictures are provided for the sailors, and on every boat that can possibly carry them motion pictures are likewise provided. And what of the people at home? What will they do and what can they do to keep their courage up, to keep their minds clear, to gain a momentary relief from the thought of horror and the thought of distress that comes so insistently from and through this terrific fight for freedom in which America is now engaged.

The honorable the Secretary of the Treasury has just publicly stated: "I should look upon it as a misfortune if moving pictures or other clean forms of amusement should be abolished."

Assuming, then, that the film-footage tax was not intended as a penalty or a license tax, it would belong in the great class of shifting taxes. But placed in that category, it meets with two very serious objections: First, it can not be shifted because of the nature of the industry; and, secondly, if it did shift, the ultimate consumer being the public, it would place a burden against one form of amusement, to wit, the motion pictures, which is essentially the poor man's, the multitude's amusement, in effect a discrimination against the one form of amusement which is undoubtedly more a necessity, more a war-time essential, than any other form of amusement known in this country at this time. And, peculiarly enough, it is a discrimination against the one form of amusement that is more economically provided than any other form of amusement. Once an actor renders his or her service before the camera, the result goes and can be made to go to entertain and diversify millions upon millions of people all over the world. In the legitimate theater the most that one actor can do in a single appearance is to entertain the number of people who can be seated in that particular theater at that particular time, which at the utmost is not over 2,000. Again, at a time when we are told that the conservation of man power is important, we find the motion-picture theater, operating entirely without stage attachés or employees, discriminated against in the tax.

The film-footage tax can not be shifted. The nature of the business makes it impossible. As presently constituted, there are three divisions of the industry—production, distribution, and exhibition. The production consists in the making of a negative similar to the plate made by the ordinary photographer, on which is reproduced the subject. In order to do this in the motion-picture industry studios must be provided and the services of actors, directors, photographers, and mechanics must be enlisted. The principal item of cost in the industry is the making of this negative, which, of course, varies in accordance with the kind and quality of picture attempted by the producer. The negative

is made on sensitized film, from which, when developed, positive copies can be reproduced practically without limitation as to number. Obviously, the cost of the negative is not in the least affected by the number of positive copies taken from it, but equally obviously the return to the producer is affected by the number of positive copies made. The positive copies are distributed for exhibition to the various motion-picture theaters on a rental basis, and the motion-picture theaters display or show the positive copies by projecting them on screens to their patrons. The ultimate consumer, then, is the patron of the motion picture, or the public. The present film-footage tax amounts to about nine-tenths of a cent per linear foot of positive, and motion-picture theaters to-day are, on the average, each exhibiting about 7,000 feet at each entertainment, the tax against which would amount to approximately \$63. As a matter of fact, however, the exhibitor does not purchase the film, merely leases it, so that the tax on each copy of 7,000 feet is divided in equal parts among the lessees. Each exhibitor accordingly pays \$1.05 of the \$63 gross tax for each day that he leases and exhibits the 7,000 feet.¹ Each copy is treated the same way, i. e., made to return its \$63 by carrying with it a charge of \$1.05 (15 cents a reel) a day against each user of it. The total revenue to the Government is brought back to the producer of the motion picture who originally pays it, according to the number of copies in use each day.

The ultimate consumer, the patron of the theater, pays no portion for the very obvious reason that such a sum can not be apportioned. On the other hand, the patron does pay the admissions tax, which is based upon the price of the ticket of admission, and in reference to which a separate brief has been prepared.

Among the peculiarities of the situation in which the film industry finds itself, it is to be noted that it is an industry which has been seriously and adversely affected by the war. Prior to the war, the producer of a negative could use it to reproduce positives for use not alone in this country, but in all of the European countries; the additional cost incurred in supplying the foreign market being only the cost of making the additional prints from the original negative, and the manufacturer derived a very large proportion of his profit from this double use of the negative. This is almost ended. Foreign countries can not use much film, but the cost of negatives remains quite as great as before, even greater in most cases because the cost of all materials as well as labor, required for the making of negatives, has increased. Further there now are no foreign negatives from which prints might be cheaply made for use here.

It is quite common to refer to the economy resulting from large output, but the economy arising from foreign use of film is of far greater moment than any saving resulting from output alone; it is the saving resulting from making the principal article of manufacture repeat its usefulness many times. The war conditions have taken it from us.

Our tax statements are before you; they show profits, although smaller, most smaller than in prewar years. But we ask you to look a little further; examine our balance sheets at the beginning and end of 1917. It will be found that we have shown profits based on inventories of film accumulated after use here and held for future use abroad; our theoretical profits are locked up in that film unless the war comes to an end soon we shall never realize that profit, as the accumulated stock of films will never be digested by the foreign market, at least not at a normal price.

We have declared these profits, and have, where possible, borrowed money to pay taxes on them. Look over our balance sheets and see to what an extent we are in debt to banks for loans to carry this stock.

It is very doubtful if any film company would have shown a profit without taking into account an inventory of film used here but capable, under normal conditions of use abroad. It is also doubtful whether film companies, in view of war conditions, are morally or legally bound to take up assets of such a risk character. We have done it, and nevertheless show profits to have been

¹ Price, Waterhouse & Co., chartered accountants, who are employed by most of the larger corporations engaged in the motion-picture business, and from whose expert knowledge and experience the figures referred to throughout this brief are taken, were deputed upon to work out the division of the tax among lessees or exhibitors of motion pictures. A payment of 15 cents a reel (1,000 feet of positive) per day equalizes the amount paid to the Government by the producers of motion pictures under the so-called film-footage tax. $7,000 = 105 \times 60$ lessees of one day each—\$63.

greatly reduced. We have paid but insignificant dividends in 1917, and none in 1918; we can pay none.

What conceivable benefits can we get from war conditions? The soldiers want films; yes, and we supply them at bare cost or below. There is a demand for film for loan and saving propaganda; we supply it free—we show films urging thrift and saving, well knowing that from that saving we shall suffer. In no way do we benefit.

As to the exact effect upon our earnings of loss of foreign trade, a concrete example may illustrate:

A certain class of negatives cost on the average, each.....	\$26, 000
50 prints for use in United States of America cost.....	10, 000
Total	36, 000
When fully used abroad, add 30 prints, cost.....	6, 000
Cost if used only in United States of America.....	36, 000
Cost if used abroad also.....	42, 000
Income from rentals, United States of America, gross.....	55, 000
Gross profits out of which to pay expenses.....	19, 000

If used abroad, the figures become:

Income from rentals, United States of America.....	\$55, 000
Income from rentals, foreign.....	33, 000
Total	88, 000
Cost.....	42, 000
Gross profit out of which to pay expenses.....	46, 000

Out of the gross profit the cost of distribution must, of course, be taken, and it is conceived that the cost of distribution in the United States of America is between 25 and 30 per cent of the gross income from rentals. The figure given above as income from foreign rentals is the net which reaches the United States, subject only to deductions to cover shipment, freight, and insurance.

The earnings are proportionate to the number of prints that can be used, this depending on territory covered.

Clearly, the business makes no war profit, and yet it is the one industry against which a penalizing tax has been imposed. Its product never reaches the consumer in the sense that other manufactured product reaches the consumer; it is never used up; it is merely shown to one set of people and then passed on to be shown to another, and the very thing that brings a revenue to the producer, the positive copy, is so excessively taxed that the producer is compelled to limit his output, and thus reduce on account of the tax, the profits on which, if earned, he would pay and gladly pay a larger return to the Government. In short, the comparatively small income derived by the Government from the film-footage tax has tended very materially to reduce the profits of the industry and so reduced the amount of income tax and excess-profits tax payable to the Government under the law. As before indicated, the film-footage tax must have been conceived out of a gross misunderstanding of the very nature of the motion-picture industry. Enforcing it is reducing the industry's contribution to the Government and placing an unnecessary and painful hardship upon both the industry and the Government.

To depart for a moment from the fundamental proposition advanced in this memorandum, the motion-picture industry wishes to call attention to the peculiarities of the law as now in force, in respect to foreign trade, which was bringing about inequitable, unjust, and in some instances unconstitutional results, with the hope that under any circumstances Congress will find in its redraft of the law adequate and proper remedies. The law provides that the quarter of a cent per foot on unexposed motion-picture stock is payable only on the raw stock which is made in America, thus exempting the imported raw stock and favoring the foreign manufacturer as against the domestic manufacturer. As a result, too, it favors the one company in America which, through its foreign affiliations, has long been in the habit of getting from its French affiliated company all of the raw stock or practically all of the raw stock which it uses for its American product. Such a discrimination being obviously unjust would seem to require no extensive argument. The law as it now stands also requires the payment of this film-footage tax by the American producer, including the quarter of a cent on each foot of unexposed and the half a cent on each

foot of exposed stock for all motion pictures exported, whether the same be made for export and directly exported by the producer or sold by the producer to domestic dealers for export. In view of the ruling of the Supreme Court in the case of *William E. Peck & Company (Inc.) v. John Z. Lowe, Jr., Collector of Internal Revenue* (decided May 20, 1918), it would seem that irrespective of any other revisions contemplated by Congress a clear provision should be made eliminating the condition last described and found by the Supreme Court in the Peck case to be unconstitutional.

If there must be in any form a tax on the American product of American producers of motion pictures it would seem clear that that tax should not be made so as to discriminate as the present tax does in any respect in favor of the foreign made, unexposed film, and it would seem, too, that the constitutional provision against the taxation of American product for export should be fully recognized and provided for in the act.

The motion-picture industry will make way for no industry, and the men and women engaged in it will make way for no men or no women when it comes to patriotism. If the Government requires the industry as a whole in the prosecution of its war work there will be no cry against the conscription; if the Government requires 100 per cent of the profits there will be no cry against that; but the motion-picture industry feels that it is justified in crying loudly and with all its power against being taxed as others are not taxed, in being discriminated against, and in being abused as it is abused under the present tax. There is no record anywhere in the world of any such tax as the film-footage tax which is now levied against the motion-picture industry. It is neither a license tax, an income tax, nor a tax against luxuries. It must be, as before pointed out, a tax created out of a total misconception of the very nature of the industry. The film is but the container of the industry's product. It is like taxing the paper in which packages are delivered from the stores, or the paper on which magazines, periodicals, and newspapers are printed.

The industry wishes to be frank and wishes to be fair. Its all is at the disposal of the Government, and it has served and is serving the Government fully, freely, ready, and anxious to do more; but just as no man falsifies his income-tax return in order to pay more by way of income tax than the Government has assessed, so the motion-picture industry feels that it should not be taxed except as other industries are taxed.

All of which is respectfully submitted on behalf of the National Association of the Motion Picture Industry, representing the entire industry in all its branches in the United States.

Dated at New York, July 26, 1918.

The CHAIRMAN. That will conclude to-day's session, and there will be no further general hearings.

[Memorandum prepared by a committee of exhibitors' branch of the National Association of the Motion Picture Industry, Alfred S. Black, chairman.]

The motion-picture exhibitors of the United States have been a unit squarely behind the administration and dedicated 100 per cent to the win-the-war program without thought of profit.

The exhibitors stand ready and glad to pay their just and fair proportion of the large amount necessary to be raised by taxation, but appeal to the Congress of the United States not to be unfairly burdened with practically the whole tax placed upon amusements to the extent that a further considerable percentage of them will be forced out of business. We desire to emphasize that as a good business proposition, it is more important to the United States Government itself than even to the exhibitors that taxation be made equitable for the many reasons cited herein.

The power of the screen in educating and affecting the morals of our people and providing the most direct means for necessary propaganda and the success of the various drives is one of the Government's principal assets in winning the war. Thousands and thousands of concrete illustrations could be given as to the cooperation and direct results obtained by our branch of the motion-picture industry in its work in connection with liberty loans, food conservation, Agriculture Department, fuel conservation, War and Navy Departments, Aircraft and Shipping Boards, Department of Interior, commercial economy board, training-camp activities, Civil Service Commission, war stamps. Re-

Cross, Y. M. C. A., Knights of Columbus, Salvation Army, Jewish war relief drives, and committee on public information, including very close cooperation with four-minute men. Everything possible should be done to encourage attendance at motion-picture theaters and nothing done to prevent same. As great as the pressing need of raising additional money by taxation, the revenue to be obtained from additional admission tax, which will undoubtedly prove so hurtful, should be of secondary consideration.

In addition to the various State and city taxes and licenses, censorship fees, etc., now being paid by motion-picture theaters, there are three distinct forms of taxation, all of which affect directly the exhibitors, two being paid by them and the third directly reducing their box-office receipts.

Tax No. 1 (seating tax): This tax was placed upon all theaters under the 1914 laws as a war measure at a time when theaters were looked upon somewhat as a luxury, and the important part they were to play in the conduct of the war not realized. Under the proposed tax the seating tax on all theaters in cities and towns over 5,000 population is doubled. If this was our only tax, we would gladly pay same without appeal.

Tax No. 2 (excise or film tax): Under the 1917 laws a tax was placed of one-fourth cent a foot on all negative film and one-half cent a foot on all positive film estimated to have given the Government a revenue of \$2,300,000. The manufacturers, not being able to withstand this tax, promptly passed it on to the exhibitors, who were even less able to withstand same, in the form of a 15-cent tax per day on each 1,000 feet of film leased, with the result that between 3,000 and 4,000 theaters were forced out of business on account of same and the other additional burdens caused by the war.

Under the proposed tax a 10 per cent tax on rentals is to be levied, which upon an estimated gross rental of \$70,000,000 amounts to \$7,000,000, or approximately three times the present revenue, and which, if placed upon the motion-picture exhibitors, will force very many more of them out of business.

The exhibitors feel that the seating tax and film tax is really a double taxation and thereby out of proportion to taxes upon other industry. That the fundamental principle of all taxation is to pass same to the consumer, in this case the general public, but that this can not be done without profiteering by increasing admission prices, which is also a dangerous procedure as seriously affecting the business itself, very largely a poor man's amusement. That production of motion pictures should not be taxed unless all productions for the amusement world be so taxed, and such tax be equitably distributed over the whole amusement field. For illustration, the production of a stage drama or musical production down to a phonograph record or baseball bat should be similarly taxed. That we admit there are many evils in the motion-picture industry which should and will be corrected in time, but which are at present uncontrollable by the exhibitors, the lessees. An especial evil is the high salaries paid by the manufacturers to the motion-picture stars. These salaries compose a very large part of the cost of production, and whereas the Government is already collecting large taxes from said stars, it is again double taxation when a percentage tax is placed upon film rentals.

Tax No. 3 (admission tax): This tax proposes doubling the present admission tax. When the admission tax was placed upon theaters under the 1917 tax law we feel the law should have been worded so that it would have been a straight 10 per cent tax upon admissions and not upon the unit of each 10 cents admission, as it would have been much more equitable and practical in its workings. That immediately upon the collection of the tax the theater attendance fell off over the United States upon an average of 25 per cent to 30 per cent, and it was some four months before its partial effect was overcome. Normal conditions have not yet been recovered and, as already referred to herein, many hundreds of theaters were forced to close.

The smaller theaters in the small cities and towns, which comprise 75 to 80 per cent of the total theaters of the United States, are having at present a hard time to get by and gradually it is getting worse for them. While a comparatively few cities and towns have been benefited by war activities, the continuous draft and other causes of the war are changing many smaller theaters from a small profit to a loss, and no additional burdens can be endured without forcing many more hundreds of theaters out of business.

If an increase of admission tax is made at the present time, it will cut down the theater attendance probably in greater proportion than in 1917, and by compelling so many theaters to close will defeat the ends desired to be obtained. The Government will get only a small portion of increased tax as esti-

mated and in turn will lose a large part of the available power of the screen and, as heretofore emphasized, at a time when we believe it very unwise for so very many reasons.

We therefore strongly urge that you carefully weigh the placing of double taxation and especially not to overburden our industry by excessive taxation and additional admission taxes so that the purposes for which the exhibitors of the United States as a unit are so earnestly working may not be automatically taken from them.

All of which is respectfully submitted on behalf of the exhibitors' branch of the National Association of the Motion-Picture Industry, representing the motion-picture theaters of the United States.

ROCKLAND, ME., *September 20, 1918.*

(Thereupon, at 12 o'clock noon, the committee adjourned.)

(The following brief was submitted by the Eastern Soda Water Bottlers' Association:)

WASHINGTON, D. C., *September 18, 1918.*

HON. F. M. SIMMONS,

Chairman Finance Committee, United States Senate,

Washington, D. C.

DEAR SIR: The undersigned members of the carbonated beverage industry, representative of 31 States, beg to submit for your consideration in connection with House bill 12863 the following:

While the tax of 20 per cent of the selling price of carbonated beverages proposed in the measure referred to heretofore is very high for the extent of the business involved, we rely upon the judgment and fairness of your committee to adjust said tax in conformity with the limitations and the needs of our industry and our country.

We respectfully call the attention of your committee to section 628, subsection (a), and suggest that the line reading "a tax of 20 per cent of the price for which so sold" be changed to read "a tax of 20 per cent of price for which the contents are sold." This is to make clear the distinction between the contents and the package where a deposit has been exacted to insure the return of boxes and cases.

We further recommend that section 628, subsection (b), be amended by the addition of the words "at 5 cents to 9 cents per gallon, a tax of 1 cent per gallon."

Your committee is also respectfully requested to consider the fact that under the present law the tax is entirely absorbed by the manufacturers of carbonated beverages and has not been passed on by the manufacturers to the ultimate consumer.

We further ask you to consider the fact that the manufacture of soft drinks has been curtailed 50 per cent in its sugar supply and that labor, and other conditions arising from the war have burdened the industry to such an extent that we must respectfully request that you consider carefully the present limited scope in levying whatever taxes your judgment may consider necessary.

Respectfully submitted.

EASTERN SODA WATER BOTTLERS' ASSOCIATION,

H. J. McMACKIN, *Secretary.*

NATIONAL BEVERAGE & MINERAL WATER ASSOCIATION.

PANNILL MARTIN, *President.*

AMERICAN BOTTLERS' PROTECTIVE ASSOCIATION,

WM. T. PHILLIPS, *Secretary.*

TO PROVIDE REVENUE FOR WAR PURPOSES.

THURSDAY, SEPTEMBER 19, 1918.

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10.30 a. m., in the committee room, Senate Office Building, Senator F. M. Simmons presiding.

Present: Senators Simmons (chairman), Smith, Thomas, Jones, Nugent, Penrose, Lodge, McCumber, Smoot, Townsend, and Dillingham.

The committee proceeded to the consideration of the bill (H. R. 11283) "to provide revenue and for other purposes."

The CHAIRMAN. The committee will hear Congressman Joseph W. Fordney, of Michigan.

STATEMENT OF HON. JOSEPH W. FORDNEY, A REPRESENTATIVE FROM THE STATE OF MICHIGAN.

Mr. FORDNEY. I will be very brief, Mr. Chairman; as brief as I can, at least.

Gentlemen, I have helped frame this bill as it is now before the House, and every member on that committee, both Republicans and Democrats, has had a free hand in the preparation of the bill. No politics have entered the committee's work at all.

I do not believe any member of the Ways and Means Committee is fully satisfied with all there is in this bill. I think never is a great bill framed where all is satisfactory to all who take part in the framing of the bill.

I reserved the right to attempt to have amended certain provisions of the bill, perfectly agreeable to other members of the committee, and I will be very brief in stating my objections to the present bill as it is now before the House.

First of all, I am not at all satisfied with the definition of capital. I think it is entirely wrong. It should be more liberal. I believe the views of the Secretary of the Treasury agree with my views in that respect. In the first place, permit me to speak of the lumber industry and mining. The raw material back of a sawmill or a mining operation measures the life of the institution and in figuring the cost or percentage in the lumber business, and I speak of that because I am more familiar with that than others, because I am a manufacturing lumber man. In the cost of production the value of

timber purchased prior to March 1, 1913, is permitted to be taken as of March 1, 1913; that is to say, if a lumberman purchased timber 20 or 30 years ago, or many years ago, at a very low price, which was the case especially in the South—20 years ago timber in the South brought 50 cents a thousand feet, stumpage, which is now worth \$5 to \$7 per thousand, stumpage; in the tree; in the woods—in the cost of production the value as of March 1, 1913, is taken and charged up to production with all other costs of production, and the difference between that cost of production and the selling price is the profit on which there must be an excess-profits tax paid or a normal tax by the corporation or the business.

Senator McCUMBER. That is, where the land itself is resold?

Mr. FORDNEY. How is that?

Senator McCUMBER. Where the land itself is resold?

Mr. FORDNEY. No; the timber cut from the land, Senator, and converted into lumber. For instance, let me give you an illustration. An average manufacturer of lumber in the South to-day is using a \$5 per thousand stumpage value and charging it to his production cost, and crediting land account with that \$5, and so on, where he has a land account on his books—and they all do—and then add to that \$5 per thousand your labor cost and all other costs, milling and planing, and so on, and all overhead costs, and the difference between the selling price and the cost is the profit.

Senator McCUMBER. That is what I wanted to get at; whether you mean the selling price of the lumber or the selling price of the lumber with the land, or both.

Mr. FORDNEY. If the land is also sold, that also must be credited to land account, and is a return of capital. That \$5 per thousand stumpage, and whatever is realized from the sale of the cut-over land, is considered a return of capital, on which there is no tax. But when it comes to the corporation asking for deductions for the purpose of paying this excess-profits tax or war-profits tax, as the case may be, under this law, that stumpage value is not permitted to be taken. The corporation must go back to the original investment, the original capital invested, surplus and undivided profits retained in the business, and so on, and that is taken as capital. Now, my contention is that the value of the production that the stumpage value of that land on March 1, 1913, or whatever you may have paid for the timber if purchased since March 1, 1913, is what is charged to the cost of production, and if so, that is a return of capital and is not subject to those super taxes, and therefore if it is capital in that instance it ought to be capital all the time. I can not see any reason why the value of your property as of March 1, 1913, when taken in the cost of production, should not be taken as capital. Now, that is the whole meat in the coconut; and for that reason I believe the value of your property as of March 1, 1913, as provided for in the act of September 8, 1916, and the act of October 3, 1917, ought to be your capital on which you ask your deductions, if a corporation or an individual. Now, that is that point.

Senator NUGENT. Are you speaking now solely with respect to the timber itself, or the land with the timber standing, or do you include also the value of the land with the timber standing?

Mr. FORDNEY. How is that?

Senator NUGENT. Do you include also the value of the land with the timber standing?

Mr. FORDNEY. Oh, yes; the value of the land should be included; whatever is received from the sale of the land, together with your stumpage value, ought to be charged to the land account, of course, as capital; and when your capital has all been returned, then, of course there is no more credit to that account. That would be true of every item of mineral. I am not familiar with oil, but it should apply also with oil.

Senator NUGENT. Would you calculate the value of the land at its stumpage value only, or at its agricultural value after the timber is removed?

Mr. FORDNEY. The value of the land should be fixed at its agricultural value after the timber is taken off. For instance, in the case of a tract I am interested in in Mississippi, when we began operations in 1907 we charged to land account a certain amount of that property. We purchased a going concern there. We charged in another account on our books, the value of the mill and all other personal property, rolling stock, and engines for logging, and steel rails and such like, and planing mill. The very first year we charged off a depreciation for the mill on this basis. When we purchased that property, upon our estimates we had 20 years' cut of timber for that mill at so much a year—40,000,000 a year.

There was nearly \$500,000 invested in the sawmill and other paraphernalia connected with it. We have charged off 5 per cent of that amount each year, so that at the end of 20 years, when our raw material is cut out, the remainder of the mill is not worth anything except as junk; whatever you get out of salvage must be credited to that account. Therefore we have charged off each year 5 per cent, so that at the end of 20 years the mill and all this other property will be wiped off our books; otherwise at the end of 20 years you have something on your books that is not worth anything, and you have not kept your books correctly. Every concern in the country does that. For instance, there is one pine-lumber company that has a mill just lately constructed, operated entirely by electricity. It was one of the first mills in the South operated by electricity. I went specially to see that mill. They invested in it \$1,000,000. They have about 12 years' cut of timber—possibly 15 years' cut of timber—in their holding. The timber in the country aside from their holding had been purchased and is in strong hands and can not be purchased by them; and when their cut of timber at the end of 15 years has been exhausted then that million dollar mill property is absolutely valueless, except for such salvage as they can get out of it; therefore they must charge off an annual depreciation, so that at the end of the operation, at the time when their timber has been exhausted, that mill will have been wiped off their books by depreciation, etc. So that it is a question of great importance, that question of depreciation.

There are 48,000 sawmills in the United States. About 28,000 to 30,000 of those sawmills are very large investments—very large mills that cut 10,000,000 or more per year. There are many sawmills in the country in which there is an investment of a million dollars in the mill and the planing mill and yards and other improvements about the place; and, as I said, when their timber has been exhausted

that property is absolutely valueless, except for whatever you may get in the way of salvage out of it.

Senator THOMAS. Mr. Fordney, why did you not fix this in your committee?

Mr. FORDNEY. My good friend, I have been fighting for it for the last two years; but my good friend Kitchin, all powerful, does not agree with me, and for this reason—and for no good reason given by himself or anybody else—if in your definition of capital you permit the use of the value of the timber as of March 1, 1913, the Government will not get as much tax from the provisions of this law as they will by charging it to an original investment—capital and surplus and undivided capital.

Senator THOMAS. Was not the report of the House committee unanimous?

Mr. FORDNEY. I agreed, Senator, that I would do as Romans do—that I would stand by the majority of the committee and offer no amendments in the House.

Senator THOMAS. And appeal to the Senate?

Mr. FORDNEY. Yes; appeal to the Senate; and I reserved that right. [Laughter.]

The CHAIRMAN. We were feeling very highly complimented.

Mr. FORDNEY. Thank you, gentlemen. I appeal to your judgment in the matter to give most careful attention to that question, because it is an exceedingly important one.

Senator NUGENT. Is it or is it not true that the lumber companies charge a proportionate depreciation of the sawmill each year to the purchaser of the lumber? In other words, do they increase the price of the lumber to the wholesaler or the retailer in an amount proportionate to the depreciation in the value of the mill?

Mr. FORDNEY. Senator, I think I could answer that by saying yes; but let me explain that no matter what your cost charges are, whether for insurance, taxes, or advertisement, or whatever the overhead expense is, must be charged to your production, and the consumer must pay it or the manufacturer goes broke. Now, whatever tax is being imposed upon the people of the country by this law—internal taxes, you as a manufacturer charge to your cost of production and you must do it or else you do not make any money. You fall behind; and the man that finally consumes that article must pay it all, and he does pay it all. Let me give you an illustration. You may say as a protectionist that would apply to imports, but it does not, because the conditions are not the same. In one instance there are two American manufacturers in competition with each other. In the other instance there are a foreign manufacturer and an American manufacturer in competition with each other, whose conditions and whose costs are not the same. That explains that.

I purchased some beefsteak at my home the other day at 50 cents a pound, and never before fully realized that whatever profit there may have been in that beefsteak, either to the farmer who raised the animal or to the butcher, all along down the line, every cost connected with it was paid by me when that beefsteak was consumed on my table; and what applies to a beefsteak will apply to a pair of shoes and every other article purchased in the country, so far as

your internal-revenue taxes are concerned, because it applies to you the same as it does to me; you and I are in the same business and in competition with each other, and we must and we do add it to our cost of production. If we do not, we are going to lose money.

Senator NUGENT. I wish you would explain a little further, if you will, Mr. Fordney, why it is that you are of the opinion that the lumber company should be allowed credit for its depreciation so far as the sawmill is concerned, if, as a matter of fact, that depreciation is charged to the customer and the customer pays each year.

Mr. FORDNEY. Well, my good friend, suppose that you purchased a million-dollar piece of property, standing timber, and you put in \$250,000 in the mill plant. You charge for your mill plant, and to your land account \$500,000, and when you commence cutting and depleting your forest and turning it into finished production you will charge for cost of production, we will say, a given sum per thousand, say \$5, and credit land account \$5. If your \$5 which you are crediting to land account is more than the timber cost you, when your land account has been wiped off your books, then you have no further return of capital from the depletion of the forest; but you must each year charge off depreciation of your mill in proportion to the life of the mill, or at the end of your operation the mill stands at \$250,000 on your books, and if you have not charged it to your customers, you are out \$250,000, because your mill is not worth anything.

Senator NUGENT. I do not understand it that way, upon your own statement. If, as a matter of fact, you charge the proportionate depreciation of the value of the mill each year to the consumers of the lumber, then at the end of 10 years, say, the mill has been paid for by the increased price that the consumer pays for the product.

Mr. FORDNEY. If you charge it off altogether; but if you do not charge it off—for instance, suppose that your cost of production is \$20 per thousand, not including depreciation as it is in the case of the company I am interested in, our depreciation being 5 per cent on \$400,000, and on the basis of a cut of 40,000,000 feet a year; that is, 50 cents a thousand feet for every thousand feet of lumber we cut. We charge that 50 cents to cost of production. Suppose that charging that to our cost of production puts the cost up to \$20.50 per thousand feet. If we do not charge that to production, our cost is \$20, but we are out 50 cents, because we can not get back that value, unfortunately; therefore we must charge to our cost each year a proper proportion of depreciation each year in order that when the business has been concluded, we shall have had a return of our capital invested in the mill. I would like to make it plainer, if I could, Senator.

Now, gentlemen, another thing. I believe, and I am sincere in this belief, after a great deal of study, that borrowed money is capital and should be permitted to be used by corporations as capital invested. Let me tell you why. Under existing law it is not permitted to be used. That is not permitted to be done. The interest paid upon borrowed money can be used as a part of your cost of production in the overhead expense. Here is an illustration: Suppose that here is a firm organized with a million dollars of capital; wealthy; their people put in all their capital, \$1,000,000.

When it comes to their deduction, they are entitled to and do get a deduction of 8 or 10 per cent, under the provisions of this law, according to whether they come under the excess-profits tax or the war-profits tax provision. They get a deduction of 8 or 10 per cent on \$1,000,000. You and I may organize a corporation for a million dollars capital, but we are unable to put in the cash. We pay in \$5,000,000 and step out and offer bonds on the property, or take any other method of borrowing money, and we borrow a half a million dollars of money. We put that money into the business. Then we have \$1,000,000 capital paid up, one-half paid by the stockholders, and the other half borrowed money; but when it comes to our deduction, we can only get a deduction of the amount of the actual cash we paid in out of our pockets, and can not get any deduction for the borrowed money. Now, that borrowed money is capital in the business; but if permitted to be used as capital in the business then there should be no interest credit for that. But whether your money is borrowed or you pay it out of your pocket, it is capital and is in the business and ought to be considered capital when it comes to your deduction.

Senator McCUMBER. Have you made an estimate of how much additional levy will have to be made to cover the losses that will follow from a change in the law making borrowed money capital?

Mr. FORDNEY. No, sir; I have not; but it would be quite an item, Senator.

Senator McCUMBER. It would wonderfully reduce the amount, would it not?

Mr. FORDNEY. It would be quite an item, there is no question. But, Senator, if we are framing a law for the purpose of getting the largest amount of money, now that is one thing; but if we are framing a law here to be just and equitable to all the taxpayers, that is another thing. You and I may be able to pass a law that will permit the collector of internal-revenue taxes to take a man by the nape of the neck and shake the money out of his pockets and say, "This belongs to the Government."

Senator McCUMBER. We should try to do both. We should endeavor to be as just as we can and get all the money we can.

Senator THOMAS. That is what your committee has been trying to do with your alternate system of taxation?

Mr. FORDNEY. To make it fair and just and equitable; yes, to all.

Senator THOMAS. Tax a man on the war-profits basis or the other basis, whichever way you can get the most out of him.

Mr. FORDNEY. That is true, Senator.

Senator THOMAS. It is like the man with his coon trap. He had it fixed "to catch 'em acomin' and agwine."

Mr. FORDNEY. The trouble is that we can not agree on all these things, and we must abide by the majority, and I will. I will vote for this bill whether I agree with it or not.

Senator THOMAS. You will not take it amiss if I criticize the House committee's bill or recommend its amendment?

Mr. FORDNEY. Oh, no. I kind of expect that, Senator. I look for it.

That question of borrowed capital is a very important one to the poor man, more especially, we will say, than to the man who has the ready cash to put in his business.

One other thing. In existing law we have the income or normal tax paid by the corporation as 6 per cent, but any money earned by the corporation and not distributed to the stockholders during the taxable year must pay a penalty, which is 15 per cent, as I recollect, unless that money is used in the business or necessary in the business; but if it has been placed to surplus by the company for the purpose of evading taxes and not used in the business, then the Treasury Department has the authority under the law to impose a penalty of 15 per cent additional. There were no penalties imposed under existing law—have been neither this year or the year before—but there is no such provision in this law. This law provides that the normal tax paid by a corporation shall be 18 per cent—a jump from 6 per cent to 18 per cent—and on such portion of the earnings of the taxable year as have been distributed to the stockholders there shall be a normal tax only of 12 per cent. Now, that is putting the cart before the horse, because the intention was to make the normal tax 12 per cent instead of 18 per cent, but that additional 6 per cent between 12 and 18 is a penalty compelling the corporation to distribute to the stockholders all of the earnings of the taxable year. Gentlemen, that is without any alternative, without any provision that if it is used in the business it is not taxable, except this.

I made so much fuss on the committee, and so many times, every day, that finally the committee agreed with me that money earned during this taxable year and used by the corporation to discharge interest-bearing obligations is not subject to the extra 6 per cent penalty. I believe it is shown that about one-fourth of the money retained by the corporations during the last year was subject to those taxes—would be subject to those taxes. If it was figured out correctly on the basis of nondistributed dividends last year, about one-fourth of that extra 6 per cent would pay the penalty. Therefore a flat normal tax of 13½ per cent would be put to 12 per cent on distributed earnings and 8 per cent on earnings not distributed.

But here is the point; here is the real test to that feature of the law, in my opinion. Every bank in the country passes each year, to surplus or undivided profits, a portion of their earnings, after the passing of a reasonable dividend by the directors.

Senator SMOOR. You mean they should?

Mr. FORDNEY. Yes; they should do it, Senator.

Now every bank in this country accumulates bad debts. I never heard of one that did not have bad debts. Finally your bank examiner comes along and orders the writing off of your books of certain bonds or notes, which are worthless, no longer valuable as assets. That bank must have undivided profits to charge that against; or it must charge that to its surplus; and under the banking laws the national banks can do that up to the limit of 10 per cent of their capital surplus, and if this prevents them from taking out of undivided profits and charging to that account, then the bank must break into its surplus, which would be a very serious matter.

Senator JONES of New Mexico. Under the proposed bill, if bad debts are found during the year, the bank has a right to charge those off against current earnings, has it not?

Mr. FORDNEY. Yes; but it must pay 18 per cent of the nondistributed dividends.

Senator JONES of New Mexico. No; I do not take it so.

Mr. FORDNEY. Oh, yes; I am correct in that Senator.

Senator JONES of New Mexico. Do they not have a right to charge off the bad debts during the year?

Mr. FORDNEY. Yes; and deduct it.

Senator JONES of New Mexico. Yes.

Mr. FORDNEY. But, Senator, whatever proportion of the earnings of the bank belongs to undivided profits or surplus during the year must pay that 6 per cent penalty.

Senator JONES of New Mexico. I understand that; but you said that you thought they ought to have the right to write off these bad debts without paying that tax, and I think they have it under the bill.

Mr. FORDNEY. No; Senator. Perhaps I have not made myself very clear.

In charging off those bad debts they must charge that to the undivided profits of the bank, which is generally a reasonable amount carried in order to take care of these accounts. Now, if they can not place to undivided profits this year any portion of their earnings without paying that extra 6 per cent, they will not put money to undivided profits or surplus and pay 6 per cent on it.

Senator JONES of New Mexico. Do not the banks now, as a usual thing, charge to profit and loss the bad debts which they have ascertained during the year?

Mr. FORDNEY. Yes.

Senator JONES of New Mexico. And then credit profit and loss with the earnings, and the balance remaining represents the earnings of the business of the year?

Senator SMOOT. Certainly.

Mr. FORDNEY. Oh, certainly; if they have nothing to charge it to but profit and loss, then they must break into their surplus.

Senator JONES of New Mexico. They charge it to the current earnings of the year.

Mr. FORDNEY. Or they must take it from undivided profits or surplus. I have been cautioned that I must stop quickly. Let me say to you the earnings of this taxable year placed to undivided profits by a bank must pay 18 per cent penalty. That is used to take care of your bad debts, of course. None can be put to surplus unless it pays 18 per cent, or to undivided profits.

Now, another thing. I will ask you to give careful consideration to these things, and if I have not made them clear you can dig it out from the bill. Here is another thing. Under existing law no person can go to the Treasury Department and get from the Treasury a report of some man's income-tax report under penalty of State prison or a fine, or both, except under Executive order. There is a provision in this law that permits the House or the Senate to call for any man's report. That opens the way for the demagogue, my good friends, and the very minute that provision is put into law the Socialists in the House or in the Senate—and we must admit that they are there; I do not know who they are, but they are there just the same—will introduce a resolution calling upon the Treasury official to furnish the tax return of some man, Rockefeller, or of the United States Steel Corporation, or the Beef Trust, or some great corporation

and any man who votes against that resolution will be immediately classed and advertised upon the billboards as favoring special interests. That information can now be obtained through an Executive order, through the President, and that is where that responsibility should be laid, and when you reach that provision in the law I wish you would be careful in your attention to that and give it all the more, possibly.

Just one more point, and I am going to conclude. This 6 per cent, imposed upon surplus, works a great hardship upon every institution in the country. For instance, I will give you an illustration on cotton mills of the country. There were in the country 33,430,000 spindles last year. There are now over 34,000,000 spindles. About two-thirds of those spindles are in the cotton mills of the South. The original cost of a cotton mill is about \$25 per spindle for the number of spindles in the cotton mill. For instance, 250 spindles cost originally about \$550,000. I think you will find in the record in my speech on this revenue bill a statement from the proprietor of a cotton mill to that effect, and that in order to do the business of the corporation, in carrying its raw material, manufactured goods on hand, customers' notes, money in the bank to meet ordinary expenses, there is required to-day a sum of money equal to the original cost of that factory, or another \$25 per spindle. At \$25 apiece, 34,000,000 spindles come to over \$800,000,000, and if you do not permit them to carry a surplus of the necessary money in order to do the business of this year, you impose a penalty upon them of 6 per cent upon between \$800,000,000 and \$900,000,000, which is over \$50,000,000 a year. That is on the cotton industry alone. The cotton industry of the South is growing like a mushroom in the night. Only 10 years ago the majority of the cotton mills of this country were in New England and in the Northern States—Pennsylvania, and so on—but the industry has been growing in the South and it is growing very rapidly, and this extra 6 per cent penalty is a mighty serious question. You will find in the record, in my remarks, a letter and a telegram from Mr. Wallace Rogers, of Mississippi, giving the necessary amount of working capital used now, and the normal amount before the war. I ask you to give careful consideration to that, gentlemen.

Senator JONES of New Mexico. Would they not be better off if they were not taxed at all?

Mr. FORDNEY. I never knew anybody that was in favor of being taxed, Senator; but we have got to pay it now. We have got to support our boys over there.

Senator JONES of New Mexico. Those that are doing patriotic work now, why tax them at all?

Mr. FORDNEY. I am in favor of taxing people, Senator, and I would make up a bill that would take more than \$9,000,000,000. This bill we are now considering will bring in from one to one and a half billions of dollars more than the estimates. The bill of last year was estimated to produce three and three-quarters billions and it has already produced over four billions; and the Commissioner of Internal Revenue says if you will give him the necessary amount of money to employ accountants to do the work, he will get more than a billion more under last year's tax, and these estimates are made upon

the same plan as the estimates made up by Mr. McCoy for the bill of October, 1917, and in my opinion will yield from a billion to a billion and a half dollars more than the estimates. If we live long enough, I hope to see that I am right about that, because I am sincere about it. I thank you, gentlemen.

The CHAIRMAN. We will now hear Mr. L. K. Leggett. What interest do you represent?

STATEMENT OF MR. L. K. LIGGETT, PRESIDENT OF THE UNITED DRUG CO.

Mr. LIGGETT. I am president of the United Drug Co., an independent interest that has not been represented at your hearings.

We are manufacturers of pharmaceutical preparations, drugs, and medicines, as well as retailers.

We are interested in sections 600 and 604; in the provisions on non-beverage alcohol.

We feel that the industry is having an injustice done it by having the tax on nonbeverage alcohol raised from \$2.20 to \$4.40 a proof gallon. It is practically the only such material that any such tax is being imposed upon. Alcohol is being used in the manufacturing of artificial spirits, artificial flowers, thermometers, brushes, and many other articles—taking them at random here—on which no tax at all is paid. That is denatured; yet our industry, in which alcohol is just as essential to the manufacturing of our products as the glassware that we put the products in, or the cork which goes in it, is taxed to this extent.

I do not believe that the committee of the House realized the importance of it or fully realized how much of a burden they were placing on our business, and I will give you just a few items showing the increased cost of some of the simple products.

Essence of peppermint, one of the commodities used in all households, has increased in manufacturing cost 31½ per cent.

Tincture of benzoin has increased 30 per cent.

Rhubarb has increased 36.8 per cent.

Cascara will be increased 29.1 per cent.

Squills will be increased 32.2 per cent.

Aconite will have an increase of 57.9 per cent.

Arnica will be increased 32.2 per cent. This affords a striking example. Iodine is manufactured under a formula by which we can use denatured alcohol, and it pays no tax at all; and yet arnica, used for almost the same purposes, in a way, will have an increased cost of 32.2 per cent; that will have to be levied on the people.

Digitalis will be increased 59.7 per cent.

Nux vomica will be increased 62.2 per cent.

Iron, quinine, and strychnine will increase 17.4 per cent.

Aromatic spirits of ammonia will increase 66.5 per cent in cost.

I illustrate this by giving you these few simple items, because they are familiar to you. That goes through the entire line of products representing some 5,000 items, in which alcohol is used.

I do not want to take up very much of your time, excepting to bear down on this one point, that the Internal-Revenue Department have so regulated the use of alcohol in medicines that they have practi-

cally made it denatured alcohol. Before we can come by alcohol it is necessary for us to ask permits of the legal representative of the Internal-Revenue Department, file with him these in duplicate, together with a bond that we will use the alcohol for medicine only. It is necessary also to file our formulas, to be forwarded with everything else to Washington. We can not buy alcohol except by designating what we are buying it for. For that reason alcohol is denatured just as much as if it were denatured physically as is the alcohol used in the arts.

I would like, if I may, to file a brief with your committee in the next day or two.

The CHAIRMAN. It will be printed, together with what you have said here.

Mr. LIGGETT. I thank you very much.

Mr. SMOOT. You had better have it in to-morrow or not later than Monday.

STATEMENT OF MR. W. M. HORNER, OF MINNESOTA.

Mr. HORNER. I wish just briefly, gentlemen, to speak to you on the question of proceeds of life insurance policies payable at death where bought purely for business purposes by an individual business, a copartnership, or a corporation.

My remarks are not in conflict with those of other gentlemen who have appeared before you to go into other phases of the life insurance question. I am glad to say to you that I am sure from an analysis that you will find out that my objection is not something that will take revenue from the Government; but if the inconsistency in section 213 is corrected, it will add revenue rather than take revenue from the Government, compared with the way it now stands.

Senator NUENT. What interests do you represent?

Mr. HORNER. The interests of a large number of life insurance agents over the country and purchasers of this form of insurance.

The paragraph in section 213 to which I wish to call attention begins on line 14 on page 9 and reads as follows:

(1) The proceeds of life insurance policies paid upon the death of the insured to individual beneficiaries or to the estate of the insured.

You will notice that that taxes income from policies payable to a copartnership or corporation. I might, just to visualize what I have in mind, call your attention to the advertisements of Wool Soap, where the shrinkage of the youngster's undershirt is shown so visibly after washing. There is also a story, which you are doubtless familiar with, or of which you will see the point if you are not—I will not prolong my remarks by telling it—a story of a colored wedding where the groom is shot and spoiled beyond recognition by the opposing faction.

Under the present law such policies are taxed through the premiums not being deducted from gross incomes. These policies, like all the policies under the new law, pay a stamp tax, and, under the proposed law, in amounts beyond \$40,000 they are counted under the inheritance tax, and taxed under the inheritance tax. This, counting the proceeds of such policies as income, the policies having paid all these other taxes, not only subjects the proceeds to the inheritance

tax, but they are counted as income which in most cases would bring them under the maximum of the surtax.

But there is another point to which your attention must be drawn, that that large amount of money, coming in in that way, brought purely as indemnity, increases the income tax that that concern would pay that year if they did not have the policy mature, so that in all cases the amounts of such policies, when they become claims by death, are shrunk into almost entire uselessness, and are almost entirely taken up by the income tax that is paid upon the insurance, and the increase of the normal tax on the normal income.

The CHAIRMAN. What amendment do you propose?

Mr. HORNER. The amendment I propose is to alter this paragraph of section 213 so that it will read:

The proceeds of all life insurance policies paid upon the death of the insured.

We just add the word "all," and strike out the balance of the paragraph, following the word "insured," in line 15.

Senator SMOOT. What is your amendment, again?

Mr. HORNER. We add the word "all," after the word "of," in line 14, on page 9, of the bill, and strike out, after the word "insured," in line 15, all the balance of that paragraph, so that it will read:

The proceeds of all life insurance policies paid upon the death of the insured.

It is not necessary for me to take up any more of your time, knowing how much you have to do, excepting to call attention to this one point. Through error in the law of 1916 the premiums paid upon such policies were allowed to be deducted as expenses, like fire insurance premiums. That created among a poorer class of agents, willing to take a spurious and temporary advantage, the recommendation to clients of insurance of a high premium kind that would not be recommended or sold or bought in normal times.

Under the law as passed last year that evil was corrected by not allowing the premiums to be deducted from gross income. Now the facts are that over these United States in the last 10 or 15 years the practice of insuring the individual in a small business as well as a large business has become general, and it is more necessary in the small business, because the small business most needs the anchorage; and the practice, I say, has grown up of putting a value upon some one or some individuals, upon the man upon whose shoulders the responsibility of that business lies, and insuring them and indemnifying the business against loss by death. It is just as legitimate as the practice of business insurance. It is of great economic value to the business institutions of this country, and it is a statement of fact that the hundreds of millions of dollars of insurance already now in force upon that plan would absolutely, necessarily, the majority of them, have to lapse. There is no reason for carrying that insurance.

Then the further statement of fact is that because of the newness of the plan, and the very low mortality of insurance in the former years, there would be very little from which the Government could claim an income, and the insurance men, not the heavy writers, but the men making a normal income, would be affected very greatly and the Government would lose rather than gain.

I thank you very much.

STATEMENT OF SENATOR JOHN WALTER SMITH, OF MARYLAND.

Senator SMITH. Mr. Chairman and gentlemen of the committee, I am here with some gentlemen to-day who represent the National Coal Association of the United States. The reason I am here, personally, is because the president of that company, Mr. Wheelwright, is from my State. Mr. Butler would like to be heard for a short time and will state what the conditions are.

Senator LODGE (in the chair). Our time is very short. Proceed.

Senator THOMAS. And we have heard a number of gentlemen upon that feature of the bill.

STATEMENT OF MR. RUSH C. BUTLER, REPRESENTING THE NATIONAL COAL ASSOCIATION.

Mr. BUTLER. You heard me on Monday, gentlemen, and a few minutes were reserved for Mr. Hornberger to discuss one subject only, that of including borrowed capital as invested capital. Mr. Hornberger has asked me to take the few minutes that were assigned to him for that subject, and I shall be exceedingly brief.

We see no reason for excluding borrowed capital from the definition of "invested capital," because it makes no difference to the business or to anyone else, really, from what source the capital employed in the business is derived. It is a mere incident of organization in many instances, that bonds are issued or notes or debentures are issued instead of stock. I can say from the history of the coal industry that the exclusion of borrowed capital from the definition of "invested capital" will strike most heavily upon the operators who are least able to afford it, namely, the men who have small companies, or the men who are endeavoring to carry on this business which is now so sorely needed for the prosecution of the war who are obliged to borrow money, not having sufficient capital of their own, with which to purchase shares of stock.

You can not classify capital. It is not divided into classes or compartments. It is for any corporation to determine what particular class of its assets are realized from the sale of bonds and what from the sale of stocks. It is all one mass, commingled, common, running together, and it is certainly more or less of an arbitrary distinction, even though Congress may have the power to make it, to say that borrowed money shall not be included in invested capital. I know of many things which are much more burdensome to a company than evidences of indebtedness of the company. I know of stock issues the protection of which is more ample and sufficient and the return on which is greater and more secure than bonds or other obligations; so that there is no reason, from the mere standpoint of the name of the indebtedness, why it should be excluded, and full recognition should be given to all classes of preferred stock.

I have asked permission to leave a brief with the committee.

Senator LODGE. It will be printed with your remarks, Mr. Butler.

(The brief referred to above is here printed in full, as follows:)

MEMORANDUM OF SUGGESTIONS SUBMITTED ON BEHALF OF THE NATIONAL COAL ASSOCIATION.

To the FINANCE COMMITTEE OF THE UNITED STATES SENATE.

The National Coal Association represents two-thirds, or nearly 400,000,000 tons, of the annual bituminous coal production of the United States. In submitting these suggestions and in the arguments presented before your committee

in its behalf, the association is looking broadly at the provisions of the bill under consideration as applicable to all lines of industry and not with special reference to their application to the coal industry alone.

We have presented three suggestions for your consideration: (1) A proposed revision of the definition of invested capital; (2) a proposal that borrowed capital be not excluded from invested capital; (3) a proposal that the excess of current cost over and above prewar cost of installations of plant, equipment, etc., be amortized at the rate of 50 per cent per annum for a two-year period.

We desire to present briefly our reasons supporting these suggestions:

(1) *Revision of definition of invested capital.* (Sec. 326, p. 61.)—The provisions of this section give no consideration whatever to the value during the taxable year of the property the income from which is subject to the tax. The unjust discrimination brought about by the provisions of the present law defining invested capital are proposed by the bill to be perpetuated and intensified. Under this section (326) the cash value of tangible property at the time of its purchase, whether 50 years ago or two years ago, is made the value of the property for the purpose of laying the excess tax. The unjust discrimination arising under the provisions of the present law are well illustrated by the table (see p. 5 hereof) presented to the committee at our hearing. The same unjust discrimination obviously will occur if the provisions of section 326 of the bill are enacted into law.

To illustrate the discrimination complained of: The table (p. 5) shows that 41 out of 395 companies reporting to the National Coal Association had for each ton of coal produced during the year 1917 an average invested capital of 65 cents upon which exemptions were allowed, and that 34 of the 395 companies so reporting showed an average invested capital of \$8.21 for each ton of coal produced during that year upon which exemptions were allowed. Allowing the maximum exemption of 9 per cent of the invested capital, as provided in the present law, the operators in the first group were credited with an average exemption of \$0.0585 per ton, and of the second group \$0.7385 per ton. It is unnecessary in this brief to discuss the reasons why this vast spread in the exemption of competitive operators selling perhaps at the same prices in the same field to the same markets exists. Merely to point out the fact is sufficient to condemn the law making any such situation possible. The remedy we propose for this discrimination is that the property subject to these taxes be valued as of the year for which the tax is levied, and if this be impracticable as an administrative matter, then that the value be fixed as of some date prior to the war, as, for instance, March 1, 1913. This proposal is in substance the same as that submitted by the Southern Pine Association and the American Mining Congress.

(2) *Borrowed money should be included in invested capital.*—Exclusion of borrowed money from invested capital under the terms of the law imposes a great hardship upon those concerns (and in the coal industry this means the concerns of smaller financial responsibility) which have found it necessary to finance their enterprises through the creation of debt. The only method of financing available to many small business men whose credit is not sufficiently established to enable them to operate upon their own capital represented by their purchase of shares of capital stock is by the issuance of bonds or other securities.

Invested capital in any business is not divided into compartments or classes. It is the common substance of the business, no matter in what manner it may have been raised. It would be impossible to separate corporate assets so as to indicate those derived from the proceeds of the issuance of stock and those derived from the issuance of evidence of indebtedness. All of the assets of any business are hazarded in the enterprise whose income is taxed under this law, and this, regardless of the source from which the assets were realized. The wide variation in capitalization per ton of production, as shown in the exhibit (p. 5), is in no small part due to the fact that invested capital does not include borrowed money, and what has been said regarding the discrimination arising by reason of the present definition of invested capital applies equally with reference to the exclusion of borrowed money from the definition.

If borrowed money be included as invested capital, it would naturally follow that interest on borrowed money should in the income tax be subjected to the same treatment as dividends on stock, that is to say, it should not be deductible from taxable income as is now provided in section 234 (2) of the bill.

(3) *The excess of current cost over and above prewar cost of installations of plant equipment, etc., should be amortized at the rate of 50 per cent per annum for a two-year period.*—The provisions of the bill recognize the principle that excessive costs due to war conditions should be speedily amortized and not carried permanently in defiance of economic principles in capital account. Limiting the rate of amortization to 25 per cent of the net

earnings, as the bill provides, will mean one thing to one company and another thing to another company. In other words, it will in practical application create unjust discrimination as between taxpayers. Furthermore, in many instances, and this is particularly true in the coal-mining industry, the rate of amortization proposed in the bill may not equal 10 per cent or even 5 per cent a year of such excess cost, as a result of which the principle of amortization for which the bill stands will be defeated by the very terms of the law itself. We suggested before the committee at the time of our hearing that subject to adjustments to be made by the Treasury Department amortization of this excess cost should be permitted at the rate of 50 per cent per annum for a two-year period. Obviously this will result in a reduction of the taxes to be paid during the two years, but equally obviously it will largely increase the taxes to be paid in subsequent years.

We believe that the limit of amortization to 25 per cent of income will work injustice in many cases, and that the power of adjustment which section 234 (8) confers on the commissioner fully safeguards the Government in this respect.

We therefore recommend that this section be amended by striking out the last sentence reading, "In no case shall deduction under this paragraph exceed 25 per cent of the taxpayers' net income as computed without the benefit of this paragraph."

In presenting the views of this association before your committee on the 16th instant Mr. Butler stated that because of the fact that the public press had announced that the Treasury Department had recommended a larger percentage of exemption for the mining industry than for any other industry, he desired to express to the committee the association's approval of such recommendation. We urge favorable consideration of the Treasury Department's recommendation for the following reasons: First, that the coal industry is said to have paid a higher percentage of its net income by way of Federal taxes for the year 1917 than any other industry, thus clearly indicating that the coal industry as an industry carried more than its share of the burden of Federal taxation; second, that the hazards of the business are relatively much greater than the hazards incident to almost any other industry.

Respectfully submitted.

NATIONAL COAL ASSOCIATION,
J. H. WHEELWRIGHT, *President*.
J. D. A. MORROW, *General Secretary*.

W. K. FIELD, *Chairman*,
A. M. OGLE,
S. H. ROBBINS,
C. E. BOCKUS,
R. H. GROSS,
J. B. L. HORNBERGER,
A. M. MARION,
W. P. HELM, Jr.,

Committee.

RUSH C. BUTLER, *General Counsel*.

Capital per ton production.	Companies reporting.		Their per cent of the production reported.	Capitalization per ton produced.			Exemption on basis of 10 per cent of capitalization.
	Number.	Per cent of total		Low.	High.	Average.	
Under \$1.....	41	10.38	19.6	0.047	0.963	0.65	\$0.085
Between \$1-\$2.....	156	39.49	27.6	1.022	1.968	1.43	.143
Between \$2-\$3.....	105	26.58	21.9	2.00	2.987	2.14	.214
Between \$3-\$4.....	34	8.61	6.3	3.072	3.979	3.46	.346
Between \$4-\$5.....	25	6.33	13.8	4.21	4.887	4.65	.465
Over \$5.....	34	8.61	10.8	5.04	1.893	8.21	.821
Total.....	395	100.00	100.00	.....	.....	2.72	.....

Capitalization of companies in first two groups representing 47.2 per cent of production (67,957,994) is \$1.16 per ton.

Capitalization of companies in first three groups representing 69.14 per cent of production is \$1.42 per ton.

Capitalization of companies in last three groups representing 30.86 per cent of production is \$5.88 per ton.

Companies reporting produce 143,894,309 tons.

The CHAIRMAN. The committee will be pleased to hear Mr. W. E. Humphrey.

STATEMENT OF MR. W. E. HUMPHREY.

Mr. HUMPHREY. Gentlemen, I wish to call your attention to one provision of the bill.

Senator NUGENT. What interest do you represent?

Mr. HUMPHREY. I represent the principal mortgage companies of the Northwest. I have here a list showing the principal ones, and I will file that with the committee.

Senator LODGE. Let it be inserted at this point.

(The list referred to is here printed in full, as follows:)

The following is a list of the companies represented by Mr. Humphrey and Mr. McConahy:

Balfour, Guthrie & Co., San Francisco.
 Seattle-American Mortgage Co., Kansas City, Mo.
 North American Mortgage Co., Bozeman, Mont.
 Northwestern & Pacific Mortgage Co., Spokane, Wash.
 International Mortgage Co., Spokane, Wash.
 American Mortgage Co., Portland, Oreg.
 Holland-Washington Mortgage Co., Seattle, Wash.
 Mortgage Co. Holland America, Seattle, Wash.
 Holland North American Mortgage Co., Seattle, Wash.
 Holland Mortgage Co., Spokane, Wash.
 Holland Texas Mortgage Co., Port Arthur, Wash.
 Netherlands American Mortgage Co., St. Paul, Minn.

Mr. HUMPHREY. I want to call your attention for a moment to a provision of the law in regard to deductions allowed corporations in the computation of their income tax in the present law. The present law provides as follows. This is a very short provision, under section 12 [reading]:

Third. The amount of interest paid within the year on its indebtedness to an amount of such indebtedness not in excess of the sum of (a) the entire amount on the paid-up capital stock outstanding at the close of the year, or, if no capital stock, the entire amount of capital employed in the business at the close of the year, and (b) one-half of its interest-bearing indebtedness then outstanding.

The present House bill changed that provision of the law, and we are simply contending that the change of the House made it a just one, and we ask that it be retained. The present House bill now being considered has this provision. I read from House Document No. 1267, Sixty-fifth Congress, second session, page 16, under the head "Deductions allowed" [reading]:

(2) All interest paid or accrued within the taxable year on its indebtedness (or, in the case of a foreign corporation, the proportion of such interest paid which the amount of its gross income from sources within the United States bears to the amount of its gross income from all sources within and without the United States) in excess of the interest received from taxation under this title.

Yesterday, I think it was, or day before yesterday, the House in Committee of the Whole struck out the last line, so that it now stops after the words "United States." That was amended, as I noticed in

looking it over, on the floor. In giving the reason for this, the report contains this statement that I think covers the whole situation in a sentence. I read from the same report, House Document No. 1267, page 92, under the head of "Deductions" [reading]:

(1) Under existing law the interest deduction is limited to interest on an amount of indebtedness not in excess of the sum of the paid-in capital stock plus one-half of the interest-bearing indebtedness. Since borrowed money is not allowed to be included in computing invested capital for the purpose of the war-profits and excess-profits tax, it seems only fair to allow as a deduction in computing net income the whole amount of the interest paid during the year.

Now, if that is proper, why should not a corporation be permitted to deduct whatever interest it is compelled to pay?

Senator LODGE. You are satisfied with the House provision?

Mr. HUMPHREY. Yes.

Senator TOWNSEND. You are satisfied with the amendment made yesterday?

Mr. HUMPHREY. Yes; with the amendment which has been made.

Senator LODGE. In striking out that last line?

Mr. HUMPHREY. Yes.

Senator ROBINSON. The amendment made in the House is not objectionable to you?

Mr. HUMPHREY. No, sir; that is what we desire. We are not perfectly satisfied with it. We could probably write one that would satisfy us a little better; but we are satisfied with that one. Take a corporation with a capital of \$400,000 and bonds outstanding of \$3,000,000; they would be permitted to deduct interest on \$1,900,000. In other words, there would be \$1,100,000 on which they were paying 5 per cent interest amounting to \$50,000, that they would not be permitted to deduct. Not only would they not be permitted to deduct it, but they would have to pay a tax on their loss, which would amount, if paying 6 per cent, to \$3,200. That is not an income or a profit. It is a tax on a loss, and, of course, there is no justice to it, and I never knew of but one reason why it was inserted in the present law, and that reason was, probably, to keep a corporation from decreasing its capital stock and increasing its bonded indebtedness. But if that was the reason, that is the only reason I can imagine why it ever did get into law; and that reason has disappeared under the excess-profits tax, because if they reduce their capital stock and increase their bonded indebtedness they would have to pay more.

Senator THOMAS. I think that was the reason.

Mr. HUMPHREY. Yes.

Senator THOMAS. And that has been one of the strongest arguments, to my mind, in favor of the British war-profits tax, which is based upon actual earnings rather than upon indebtedness.

Mr. HUMPHREY. I think that was probably a reason; but if you take it under the present law, even if you do not increase the excess-profits tax it would be a great loss for them to do it, so that there is no longer any reason that I can imagine why the provision in the House bill should not be adopted. Certainly there is no justice in compelling a corporation to pay a tax on its loss. I see no reason why a corporation should not be treated exactly the same as a natural person.

I should like to file a brief.

Senator LODGE. File your brief and it will be printed with your remarks.

Mr. HUMPHREY. That you.

(The brief of Mr. Humphrey is here printed in full, as follows:)

WASHINGTON, D. C., September 18, 1918.

Hon. F. M. SIMMONS,

Chairman Committee on Commerce, United States Senate.

MY DEAR SENATOR: Representing the principal mortgage companies of the Pacific northwest, we call the attention of your committee to the following deductions allowed corporations in the computation of income tax in the present revenue law:

The revenue act, approved September 8, 1916, under the head of "Deductions," section 12, contains the following provision:

Thrd. The amount of interest paid within the year on its indebtedness to an amount of such indebtedness not in excess of the sum of (a) the entire amount of the paid-up capital stock outstanding at the close of the year, or, if no capital stock, the entire amount of capital employed in the business at the close of the year, and (b) one-half of its interest-bearing indebtedness then outstanding.

The present revenue bill H. R. 12863, reported to the House of Representatives September 3, 1918, and as amended in the Committee of the Whole, under the subhead "Deductions allowed," section 234, contains the following provision, to-wit:

(2) All interest paid or accrued within the taxable year on its indebtedness, or, in the case of a foreign corporation, the proportion of such interest paid which the amount of its gross income from sources within the United States bears to the amount of its gross income from all sources within and without the United States.

Under the present law, a corporation is only permitted to deduct the interest on indebtedness not exceeding the sum of the paid-in capital, plus one-half of the interest-bearing indebtedness outstanding at the close of the year. This is an unusual and, it appears to us, an unjust law. Why should a corporation be subjected to a different rule, in the payment of tax, from a person? Why should not a corporation be allowed to deduct from its income all the interest it is compelled to pay? As to how the present law works and the injustice of it, take the following illustration. A corporation with—

Paid-up capital.....	\$400,000
No profits available for distribution.	
Bonds outstanding \$3,000,000, one-half deductible.....	1,500,000
Total amount on which interest may be deducted.....	1,900,000
Amount of bonds outstanding.....	3,000,000
Amount on which interest may be deducted.....	1,900,000
Causing a loss of interest on.....	1,100,000
Amounting at 5 per cent to.....	55,000

So that under the present law they are not allowed, in figuring their income tax, to deduct as an expense the item of \$55,000 paid by them in interest, but are obliged to pay a tax of \$3,300 on that amount, which is not income or profit but expense; and as there is no income or profit out of which it can be paid, it must be paid out of capital, and is not an income tax but an excise tax.

The unjustness in the operation of the present law is so apparent from the above illustration that further argument is unnecessary, for it results in compelling a corporation not to pay a tax on its income but compels it to pay a tax on its loss.

Taking the larger view of the question, the purpose of an income tax is to collect a tax upon an income or upon a profit, the same to be paid out of the profit and not to compel the payment of a tax upon a loss, which, it is self-evident, could not be paid out of a profit but would have to be paid out of the capital.

This law can not be justified on any principle of taxation and the only reason for its justification, if any, in incorporating it into the law of 1916, was to prevent corporations from decreasing the amount of their capital stock and increasing the amount of their bonded indebtedness in order to secure the additional interest allowance. But such reason, if it ever existed, has ceased.

for under the excess-profits tax law there is no longer any inducement for a corporation to take such action as they would thereby be losers, as shown by the following illustration:

Take, for example, a company operating with a capital stock of \$1,000,000, and a bond issue of \$1,000,000, drawing 5 per cent, which made a profit of 9 per cent in 1917 (\$90,000), and averaged 9 per cent for the prewar period. If they reduced their capital to \$100,000, and increased their bonded indebtedness to \$1,900,000, they would be allowed an additional deduction on income tax of 5 per cent on \$900,000, or \$45,000, leaving a balance of \$45,000 profits on which the tax would be assessed, resulting in a net advantage of \$2,700. This, however, would leave a net profit of 45 per cent on their reduced capital, which would subject them to the payment of the excess-profits tax.

With a net profit of.....	\$45,000
Allowing a deduction of 9 per cent.....	\$9,000
Specific deduction of.....	3,000
Making a total deduction of.....	12,000

We have a balance of profits of..... 33,000

subject to the excess-profits tax, which would amount to \$14,400, or \$11,700 more than the saving of \$2,700 in the income tax; or, in other words, they would lose \$11,700 by the transaction.

We therefore submit that corporations should be allowed to deduct all interest paid or accrued within the taxable year.

We submit the foregoing, confident that in view of the above facts, your committee will approve the provision in reference to this matter in the present House bill.

Respectfully submitted.

W. E. HUMPHREY.
JAS. M. MCCONAHEY.

STATEMENT OF MR. O. F. HIEMKE, SECRETARY OF THE AMERICAN APPRAISAL CO., MILWAUKEE, WIS.

Mr. HIEMKE. Mr. Chairman and gentlemen of the committee, I wish briefly to submit to you for consideration the provision of section 303 of title 3 of the war and excess profits tax, which provides as follows [reading]:

SEC. 303. That in the case of a corporation the earnings of which are to be ascribed primarily to the activities of the principal owners or stockholders who are themselves regularly engaged in the active conduct of the affairs of the corporation, and in which capital (whether invested, borrowed, rented, or otherwise secured) is not directly or indirectly a material income-producing factor, there shall be levied, collected, and paid for each taxable year upon its net income (in lieu of the tax imposed by Title II of the revenue act of nineteen hundred and seventeen and in lieu of the tax imposed by section three hundred and one of this act, but in addition to the other taxes imposed by this act) a tax of twenty per centum of the amount of its net income in excess of \$3,000. A foreign corporation shall not be entitled to the specific exemption of \$3,000.

A corporation fifty per centum or more of whose gross income (as defined in section two hundred and thirteen for income-tax purposes) consists of gains or profits derived from purchase and sale, or of gains, profits, or commissions derived from Government contracts, or whose invested capital is more than \$100,000, shall not be subject to the tax imposed by this section, but shall be subject to the tax imposed by section three hundred and one.

I should like to speak of the corporations mentioned in the last paragraph I have quoted from this section. "whose invested capital is more than \$100,000."

Briefly, the American Appraisal Co. was organized 20 years ago by its present president and treasurer, and it was merely incidental that the form of organization was a corporation. Up to the present date

not a dollar has ever been paid into the treasury of the American Appraisal Co. for its capital stock.

As secretary of the company, I have been connected with the company for 16 years, and the other dozen who are with the company have practically all been with the company for more than 15 years, so that we are an organization of highly trained and expert appraisers.

Senator THOMAS. What is your business? What do you do?

Mr. HIEMKE. We make appraisals of properties for financial purposes, for insurance purposes, upon which to base insurance and collect the losses after a fire. We are a disinterested authority, and have been accepted as such in the purchase and sale of large properties, in the settlement of fire losses, and in many other activities where disinterested valuation is desirable.

Senator THOMAS. Your assets consist in your experience and—

Mr. HIEMKE. Yes; our assets are our experience, an accumulation of 20 years in a successful enterprise.

Senator JONES of New Mexico. What would you say to inserting in the law a provision treating such a corporation as a partnership?

Mr. HIEMKE. That is exactly what we would like to submit to your honorable body for consideration.

Senator THOMAS. In connection with that, what have you to say to our extension of this law so as to include partnerships and individuals?

Mr. HIEMKE. I beg your pardon?

Senator THOMAS. I say, in that connection, what would you have to say regarding the expediency of extending the clauses regarding excess-profits and war-profits taxes to partnerships and individuals? It is now confined to corporations.

Mr. HIEMKE. I do not know.

Senator JONES of New Mexico. It is extended under the excess-profits tax.

Senator SMOOT. Not under existing law.

Mr. HIEMKE. Not under the present law; and that is why we would like to have considered the reasonableness or equity of having eliminated those words limiting it to a capital of \$100,000 for such concerns as ours; and I know there are others in the country, but I have been in Washington only 36 hours, and I came immediately on ascertaining that provision in section 303.

Senator ROBINSON. Do you desire to submit a specific amendment which would accomplish the specific purpose?

Mr. HIEMKE. I have framed a letter which I would like to ask permission to submit in the record, and I would like to ask consideration of the feasibility of eliminating that provision the same as the provision with regard to individuals and copartnerships has been eliminated from the excess-profits tax.

Senator SMOOT. How do you do in your company—just issue one share to each of the individuals interested?

Mr. HIEMKE. We are capitalized for \$300,000, and we have about \$250,000 issued to-day, with the balance of the stock in the treasury, contracted with worthy employees, which will be paid to them annually in consideration of their staying with us a number of years. Those old employees are our asset, and we are issuing to those em-

ployees, in addition to their salaries, as an incentive to remain with the company, this stock.

Senator SMOOT. Then the company has not received anything in cash for the shares issued?

Mr. HIEMKE. The company has up to date not received one dollar for any of the shares that are issued, and we have no capital. Our surplus and undivided profits conduct our business, and that money is merely used as an incident to the business to provide for deferred payment for services rendered or to provide for office furniture. We do no merchandising, no manufacturing, or trading of any kind; simply render our service as a copartnership or individual would. But because of our organization, and because this organization has been a successful institution with the members who founded it, we would be subjected to what we believe is an unjust provision of the law if that \$100,000 provision is allowed to stand, and an unfair advantage to any other organization who would have, say, \$90,000 invested in their business. They would pay 20 per cent, and we would pay, under the excess-profits tax or the war-profits tax—and our business is of such a nature that it would come largely—up to 80 per cent of our earnings. We are willing to pay and anxious to pay all the taxes that are equitably imposed, and if the law could be framed so that an organization such as ours would pay 20 per cent tax we would be highly pleased, but we do submit for your consideration the elimination of that as an unjust provision to organizations such as ours.

Senator JONES of New Mexico. Do you pay salaries to all of these members?

Mr. HIEMKE. Yes, sir; all officers are paid salaries, and profits are declared on the stock as the stock is issued, as dividends.

Senator JONES of New Mexico. Do you pay salaries, do you think, commensurate with the worth of the services, or are they merely nominal salaries?

Mr. HIEMKE. That is a hard question to answer. I would say that the salaries and the stock issued and dividends represent and are commensurate with the services rendered by the respective members.

Senator JONES of New Mexico. And that includes dividends as well, you think?

Mr. HIEMKE. Yes.

Senator JONES of New Mexico. Do you object to telling us how much the salaries of these different people are?

Mr. HIEMKE. I would be glad to. The president receives \$25,000 a year; the treasurer receives \$20,000; the secretary, \$16,000; the vice president, \$15,000; the general manager, \$15,000; the general superintendent, \$11,000; and the assistant general manager, \$4,641.66.

Senator JONES of New Mexico. And how much will be added to those sums by way of dividends?

Mr. HIEMKE. That depends upon what dividends are declared.

Senator JONES of New Mexico. What has been your experience?

Mr. HIEMKE. They have ranged from nothing up to 75 per cent. Last year they were 75 per cent. The year before that they were 40 per cent.

Senator SMOOT. That is 40 per cent of the stock that is issued to them, or 40 per cent more than the salaries they are paid?

Mr. HIEMKE. Forty per cent on the stock that is issued to them, to the stockholders of record.

Senator NUGENT. What addition would that make to the salaries that you have enumerated there, in dollars and cents, approximately; if you desire to give that information?

Mr. HIEMKE. It is 75 per cent on \$237,950 at the close of our last fiscal year, February 28, 1918.

Senator JONES of New Mexico. What proportion of that does your president get?

Mr. HIEMKE. The president has 805 shares.

Senator ROBINSON. What is the par value of the shares?

Mr. HIEMKE. \$100.

Senator ROBINSON. I think we could figure that from the statement you have made.

Mr. HIEMKE. I could compile that and submit it.

Senator JONES of New Mexico. I wish you would, and just put it in in connection with your remarks.

Mr. HIEMKE. Yes, sir.

(The statement referred to is here printed in full, as follows:)

WASHINGTON, D. C., September 19, 1918.

Hon. F. M. SIMMONS,

Chairman Senate Finance Committee,

Washington, D. C.

DEAR SIR: The proposed revenue bill for 1918, which you have now under consideration, draws an unfair discrimination in section 303 between corporations having more than \$100,000 invested capital and smaller corporations, copartnerships, and individuals engaged in an identical or a similar business; that is, that of rendering personal services.

In the fourth line of the second paragraph of section 303 of the proposed law, corporations having more than \$100,000 invested capital are made subject to the taxes imposed under section 301 which might amount to 80 per cent of the net income, if computed under the war-profits method, and to the graduated scale of taxes if under the excess-profits method, whichever produces the most tax.

Smaller corporations though engaged in the same work are only taxable at the rate of 20 per cent upon net incomes in excess of \$3,000, while copartnerships and individuals are not subject to any excess-profits or war-profits tax under the proposed bill.

The American Appraisal Co., of Milwaukee, is a Wisconsin corporation with authorized capital stock of \$300,000. Not a dollar has ever been paid into the treasury of the company for stock, all the stock issued to date having been issued for good will or bonuses for services rendered by the stockholders.

Mr. J. L. Moon and Mr. W. M. Young, present president and treasurer, respectively, founded the corporation 20 years ago, and the writer has been associated with the corporation for 16 years. The dozen smaller stockholders have practically all been with the corporation for 15 years or more.

At the end of our last fiscal year, February 28, 1918, Mr. J. L. Moon held 805 shares of stock, par value \$100; Mr. Young, 586 shares; and the writer, 358 shares, the balance of 630 issued shares being held by the 11 smaller shareholders.

The corporate form of our association of expert appraisers is clearly incidental only to our organization. Its business consists of rendering expert personal services in making appraisals of industrial and other establishments for financial and other purposes, which calls for a high degree of technical training and experience. Its earnings have always been and are now primarily due to the activities of the principal stockholders or owners, to whose industry and efficiency the development of the business may be ascribed. We are not a manufacturing corporation, do no buying or selling or any kind of merchandising, and the use of capital in this company is purely incidental to the character of the personal services rendered, being necessitated by delay and irregularity in the receipt of fees, advance of salaries, wages, providing office equipment and accommodations.

Under the existing revenue law businesses rendering personal services, such as the American Appraisal Co., and as above outlined, are taxable upon excess profits at the flat rate of 8 per cent, without regard to the form of organization, whether corporate or a partnership or individuals, and without regard to the volume of business or size of capital.—Articles 71 and 72, regulations No. 41, Treasury Department, United States internal revenue, section 209 of the act.

While the 20 per cent flat rate upon such corporations as ourselves is quite agreeable, I submit that it is not equitable to impose such a tax discrimination in the same businesses because of the form of organization or because of the size of invested capital, when with such discrimination a heavy burden is placed upon the existence of the one and an unfair advantage is given to the other class.

To do justice to such cases as ours the \$100,000 limitation of invested capital should be stricken from the bill, which is the relief we are herein seeking of you.

It should also be borne in mind that the stockholders as individuals will pay increased normal and surtaxes upon their personal incomes, practically all of which are derived from this corporation.

In conclusion I wish to express my appreciation of the courtesies extended by your committee and bespeak your further kind consideration.

Respectfully submitted.

O. F. HIEMKE,

Secretary American Appraisal Co. of Milwaukee.

Senator TOWNSEND. Mr. Chairman, a matter was brought to the attention of the Committee on Ways and Means with reference to insurance—the tax on unauthorized insurance companies. Mr. Rainey, a member of the committee, wrote a letter to Mr. Doyle, a member of the Board of National Fire Underwriters, stating the position and asking for information, which Mr. Doyle furnished in a letter, and submitted a proposed amendment to the bill. I would like to have that put into the record here now, in order that we can ask the Treasury, or the Treasury Department, when it comes in, because it appears that it was opposed to a matter that appears to me to be absolutely just and fair.

Senator LODGE. It will be printed in the record at this point.

(The letters referred to are here printed in full, as follows:)

JUNE 26, 1918.

Mr. J. H. DOYLE,

*National Board of Fire Underwriters,
76 Williams Street, New York City.*

MY DEAR MR. DOYLE: We are engaged in framing, as you know, a very large revenue bill. It is necessary to find every possible source of taxation. I am advised that there are policies of transportation and marine insurance which were issued by companies having no place of business in the United States, and these companies, therefore, are not amenable to our taxing laws, neither national nor State. They are in direct competition with our domestic companies and are also in direct competition with those foreign insurance companies which have complied with our laws and which have a domicile in the United States, and which are subjected to the license requirements of our States and our State taxing systems, as well as our national income taxes, etc. I wish you would advise me as to the extent of this business.

Also, advise me as to the total amount of premiums which go abroad in insurance of this character. I understand the situation to be that vessels and their cargoes are to some considerable degree insured directly by the owners, who make their applications direct to a foreign country. I would like to know how much this amounts to. I am also advised that a good many foreign companies having a domicile in the United States and authorized to do business here sometimes refer business of this character to their home offices, and the business is conducted by mail or by cable between the home office and the person taking out insurance on a vessel or floating structure of some kind, or its contents, in this country. Do you think there is any foundation for a suspicion of this kind?

I will be very glad, indeed, to have any data you can send me as to the character of the insurance business I am discussing in this communication.

Very truly, yours,

HENRY T. RAINET.

THE NATIONAL BOARD OF FIRE UNDERWRITERS,
New York, June 28, 1918.

Hon. HENRY T. RAINET,
House of Representatives,
Washington, D. C.

MY DEAR CONGRESSMAN RAINET: We are in receipt of your favor under date of June 26, in relation to the proposed revenue bill.

Your information respecting placing of insurance by persons, firms, etc., in the United States with foreign companies is unquestionably correct. There is a very great volume of this business placed in companies and associations not authorized to transact business in the United States, and such companies share none of the expense of our national, State, or municipal governments, nor are the policies taxed under the provisions of the present revenue act. Their activities are not confined exclusively to marine and transportation risks, but include all classes of property insurance; that is, fire, fire, tornado, bombardment, invasion, etc., in addition to transportation and marine.

These companies make no returns to any taxing authority in this country, and it is impossible to do more than estimate the amount of the premiums. I have conferred with a number of our leading insurance officials and they assure me that a conservative estimate of marine and transportation business would be more than \$50,000,000 annually, and that other property risks combined will exceed the amount paid for marine and transportation. If this is true, and I believe it is, a conservative estimate of the total business would indicate a minimum of \$100,000,000 annually. Of this immense sum nothing is contributed to the support of either our national, State, or municipal governments, and the business is in direct competition with our domestic companies and the United States branches of foreign companies.

It is the general belief that the opportunity presented to foreign companies having United States branches to evade payment of any taxes in this country by transacting business direct from the home office is so apparent that many have availed themselves of same. In this practice I am quite sure the United States branches take no part, but the business is written at the home office abroad, at the instance of the assured or some broker acting for him, and the authorized branch in this country has no record or knowledge of it.

I understand the modus operandi of handling this business by foreign companies is to issue policies covering property in this country, basing their liability upon that paid by some American company covering the same risk. To illustrate: They will issue a policy for \$10,000 with a provision that they are liable and will pay upon the same basis at the same ratio and in like amount to the blank insurance company which is interested in the risk. By this means they not only escape the item of tax expense, but likewise escape the items of expense of adjustment, inspection, etc., and have but a small acquisition cost.

In a competitive way they have a further advantage of being immune from the application of our various State laws affecting the business of insurance, such as antidiscrimination in premium charges, the necessity for having policies countersigned by a resident of the State upon whom service of process may at any time be had, and the numerous other restrictive measures to be found in the statutes of the various States. They can charge one firm one rate and another firm under conditions almost identical an entirely different rate. Domestic and authorized companies are not permitted to discriminate in this manner and the result is that in a competitive way the foreign interests have a tremendous advantage and secure business through the very simple process of taking advantage of the rate which domestic companies must maintain to prevent discrimination.

This class of business, therefore, could bear a very much heavier tax than that imposed upon the premiums of domestic and authorized companies. I should say that a tax at the rate of 10 per cent upon insurance covering property interests placed with foreign companies not authorized to transact business in the United States, or if authorized, not placed through United

States branches, would secure for the Government annually a sum in excess of \$10,000,000. This would not result in an increase in rates, as the items of the several taxes now imposed, plus necessary expenses which the domestic and authorized companies must bear, are in excess of the 10 per cent you mention.

All of the above is confirmed by the estimates of several of our larger companies based upon their competitive experience.

Trusting this is the information you desire, I am,

Yours, very truly,

J. H. DOYLE,

Assistant General Counsel.

INSURANCE.

[Proposed amendment.]

Each policy of insurance, or certificate, or binder, or covering note, or memorandum, or cablegram, or letter, or other instrument by whatever name the same shall be called, by which insurance shall be made or renewed upon property of any description (including rents and profits) whether against peril by sea or on inland waters, or in transit on land, or transshipments and storage at terminal or way points, or by fire, lightning, tornado, windstorm, bombardment, invasion, insurrection, riot or other peril taken out by or on behalf of a citizen of the United States or a resident thereof, or by any corporation or partnership created under the laws of the United States or of any State, Territory, or district thereof, a tax upon the amount of premium charged of 10 cents on each dollar or fractional part thereof.

Provided, That this tax shall not apply to any policy or other instrument issued by an insurance company created under the laws of the United States or of any State, Territory, or district thereof, or by any person, partnership, or association of persons residents of the United States and duly authorized to engage in the business of insurance under the laws of the United States or of any State, Territory, or district thereof; nor to any policy or other instrument issued by any insurance company or corporation not created under the laws of the United States, or of any State, Territory, or district thereof, or by any person, partnership, or association of persons not residents of the United States when such foreign insurance company, corporation, person, partnership, or association of persons is duly authorized to engage in business under the laws of the United States or of any State, Territory, or district thereof, and such policy or other instrument is written, signed, and issued by such company, corporation, person, partnership, or association, or its duly authorized agent in the State, Territory, or district of the United States within which it is authorized to do business: *Provided further*, That policies of reinsurance shall be exempt from the tax imposed by this subdivision.

It shall be the duty of every person, partnership, firm, association, or corporation (including brokers and solicitors) procuring a policy or other instrument by which insurance is made or effected, or acting for or on behalf of any other person, partnership, firm, association, or corporation in the procurement of such policy or other instrument and which is taxed under the provisions of this subdivision, to attach and cancel to each of said policies or other instruments a stamp or stamps equal in value to the tax imposed thereon by this subdivision.

The CHAIRMAN. The committee will next hear Mr. Oren B. Taft.

STATEMENT OF MR. OREN B. TAFT, PRESIDENT OF PEARSONS-TAFT LAND CREDIT CO., CHICAGO, ILL.

Senator LODGE. Whom do you represent?

Mr. TAFT. I represent the Illinois State Bank and the Pearsons-Taft Land Co., of Chicago, Ill., and others like interested, and what I have to say may have been said repeatedly. In a word, if I can confine it to that, section 303 was evidently intended to meet our case, being a corporation where the stock is largely held by the officers who are actively engaged in the business and have been all their business life; but our capital is \$200,000, the minimum allowed by the statutes of Illinois for State banks. We can not reduce it to meet

this proposed law, and would like to have the proposed law increased to at least \$200,000. That will meet our case. As to a larger amount, that is subject to your own judgment. If that is done it meets all that we need. Without that or another amendment which I will suggest, where the House evidently has intended to meet our case, they have failed, perhaps they not understanding the concrete case, because between \$100,000 and \$200,000 we are left as we were before, which was this: We have been a business organization going since 1866. I have been continuously in the business myself since 1869. It has been owned and operated very largely as a business, first as a partnership and then as a corporation, by two individuals, my former partner, an official, and then myself and my sons.

In 1912 my former partner went out of the business, and my sons purchased his stock, paying \$400 a share for it in money. That is the basis and the evidence that we have—and the business has not changed in its character since—for the value of our capital invested.

Last year we paid a tax beginning with an allowed exemption of 8 per cent on \$200,000, or \$16,000. Had we been capitalized as we might have been, had there been a need, we would have been capitalized for \$800,000 of actual money on the basis of evidence that would be satisfactory to any official representative. In that case we would have started with a proper exemption of 7 per cent on our \$800,000, or \$56,000. Between those two points of \$16,000 and \$56,000; that is, we paid a tax on \$40,000, because we happened to be incorporated for \$200,00 instead of the actual fair value of our stock, \$800,000.

Now, had section 303 read \$200,000, or an amount more but not less, I, if it were to become a law, have nothing more to say. We are ready to pay whatever tax Congress puts upon us; and I mean that. None of us have yet gone into our principal, and we ought to before we get through with this case.

My only suggestion is that you incorporate into this proposed law the provision in the capital stock which provides for the ascertaining of a fair stock value. It has all of the working method; it accomplishes the purpose by ascertaining, and it is known to you by ascertaining what is a fair value of the stock as capitalized upon the earnings for the past five years. Take our earnings for the past 5 years, if you please, and we are willing to abide by that; or the last 10 years or 15 years, and take the total for the 5 years and divide it by 5, giving the annual net earnings for the last 5 years. Capitalize that, if you please, at 8 per cent, which is the suggestion in the internal-revenue commissioner's suggestion—capitalize that at 8 per cent and give us that capital and put us under any method of taxation, excess-profits tax, or war-profits tax that you please, and we will pay the tax. All we ask—and I know that you want to grant it, and I believe the House has indicated its desire to grant it—is a fair start at the bottom upon a fair value of our stock, with a fair pro rata equitable exemption with the rest, and other corporations of a like character, and then tax us according to your excess-profits tax or your war-profits tax, and we will pay it. We ask that we be given a chance to start with an exemption in equity and equal with others. I have said it all. Has it been covered? If not, can there be any objection? We have no provision

in the proposed law by the House which does not leave us precisely as we were under the law last year.

Senator McCUMBER. Do you not think that all taxes should be levied upon the actual invested capital during the year of taxation rather than upon stock?

Mr. TAFT. Senator, there appears to be an attempt to define invested capital, and this law goes into definitions.

Senator McCUMBER. If we would go outside of that definition and provide that the tax should be levied in all cases upon the actual capital employed during the taxable year we would avoid your objection?

Mr. TAFT. Yes, sir. If you were going into our office for the purpose of buying our business, I do not think you or any member here would have any difficulty in ascertaining what that was worth in dollars and cents. That is all we ask; use the business method. The reason, as near as I can read it into the House bill, is that they do not know what to do with good will as a value—and I do not. You can play horse with it if you please, and I think they have dodged it and are afraid of it. I should imagine so. There is a way to determine what that good will is. If the organization has been in business long enough to establish its own record according to its own books so as to show the earnings, then capitalize the earnings on whatever basis you please or fix as fair, and you have got the answer. The House bill does not do that. It puts good will in the intangible assets. All right. I can understand why; patent rights; contracts; possibilities; good will.

Senator JONES of New Mexico. Let me see if I understand your suggestion. You would take a given business and estimate the amount of profit which it ought to earn on capital in the particular business?

Mr. TAFT. Precisely.

Senator JONES of New Mexico. Well, take that earning at 8 per cent, and then if its earnings are \$8,000 you would estimate the invested capital at \$100,000?

Mr. TAFT. Precisely.

Senator JONES of New Mexico. If you take some other line of business where you would expect to earn 10 per cent and it earned \$10,000, you would have the invested capital at \$100,000?

Mr. TAFT. Senator, I thought I had something here that would show you, but I find I have not.

Senator ROBINSON. You would not take the actual earnings, then?

Mr. TAFT. I would take the net earnings. As you say, you can make net earnings mean anything. I can make my salary three times what it ought to be.

Senator ROBINSON. That is what I was getting at.

Mr. TAFT. The internal revenue have issued instructions by which to reach that very thing.

Senator ROBINSON. You say you would take the net earnings as the basis of capitalization?

Mr. TAFT. Yes.

Senator ROBINSON. And you can make the expenses anything you want to?

Mr. TAFT. Yes.

Senator ROBINSON. So that you would reduce the net earnings to any amount you might care to?

Mr. TAFT. Yes.

Senator ROBINSON. Then the amount of cash that the concern would pay would depend entirely upon the amount of expenses it incurred. Then, by paying themselves enormous salaries, why could not the owners of a corporation prevent the Government from receiving any tax at all? Why could not they pay out the total gross earning and have no net earnings and pay no tax?

Mr. TAFT. They can do exactly what you have suggested, and so the Treasury Department have endeavored to meet it and they do meet it. Why do I say they do? Because ever since you have had a revenue law your Government officials have come into our bank and have spent at least three days there going over these very items, allowing this and refusing that, and your internal-revenue instructions are right to that point.

Senator ROBINSON. Would you give the Government the power to fix the salaries of the officers?

Mr. TAFT. It gives the Government the power to come in and report to the headquarters whether they are excessive or not. That is merely a regulation which, as I say, comes in the revenue act.

As I was going to say, you can not meet it except in one way. You can not fix the salaries. You have got to determine in some way what shall be permissible and what is not. In other words, answering Senator Robinson's question, I know of no way—I would know of no way if I were sitting in one of these chairs—by which to determine what my salary shall be in the concrete; and yet, in every case, the concrete has got to be the answer in that particular corporation. For instance, in my case I retired from active business; that is, I gave up my office hours, and my two sons are running the business as I did before them, and acting merely as advisor and to keep the thing running when it is in danger—and I am there every day—my salary is \$9,500 a year.

Senator ROBINSON. What was it before you retired?

Mr. TAFT. \$12,000. My sons each receive \$10,000 and give all of their time, and I am quite ready to say that they can earn 50 per cent more than that and get a position in a week's time any time. They are thoroughly capable and are managing a business that handles millions of dollars. Our salaries are certainly reasonable. Can I say anything more on that?

Senator ROBINSON. I think I understand your position.

Senator TOWNSEND. I do not understand that you have answered Senator Robinson's question when he said you were going to base your capitalization upon your net profits and that you can make those net profits anything you choose.

Senator ROBINSON. That means you can make your tax anything you choose, and that is exactly what we want to get away from.

Senator LODGE. Mr. Taft, I do not want to cut you off, but the Senate has come into session; it is 12 o'clock, and a brief executive session of this committee is desired.

Mr. TAFT. May I file anything by sending it to the committee?

Senator LODGE. Yes.

Mr. TAFT. I can do it within a day or two. I have one or two suggestions in connection with sections 303 and the \$200,000.

Senator LODGE. Get here before Monday whatever you desire to go into the record. Any amendment or argument that you desire to make will be printed with your statement.

Mr. TAFT. Thank you.

(The brief referred to by Mr. Taft was subsequently submitted and is here printed in full, as follows:)

BRIEF SUBMITTED IN CONNECTION WITH REMARKS BY OREN B. TAFT, VICE PRESIDENT OF PEARSON-TAFT LAND CREDIT CO., A STATE BANK LOCATED IN CHICAGO, ILL.

All references herein are to House bill 12863, with Chairman Kitchin's report attached.

Following amendments are suggested:

1. To section 327:

"(4) Where corporations are engaged mainly or exclusively in farm or real estate mortgage investment banking business and derive their income mainly or exclusively from parts of interest paid on the mortgages sold by corporations."

This should go in just above the last line on page 28. Then amend provision (b) of said section 327 by inserting the words "first three" before the word "cases" in the first line of the subdivision and add at the end of the subdivision (b) the following: "In the fourth case specified in subdivision (a) the minimum invested capital shall be one-twentieth of the aggregate amounts of principal in the mortgages contributing during the taxable year to the income of such corporations."

It is believed the fairness of these amendments will impress you and anyone else familiar with such concerns as ours. In our own case with these amendments in the law our capital actually invested would be about \$700,000; our excess profits credit, \$59,000; and our tax about \$18,000, leaving the net return to the stockholders on the purchase price of their stock about 6 per cent.

The amendments suggested have the merit of being simple and easily applied and of no broader application than the few cases specified therein.

The character of the business in the cases provided for by these proposed amendments is based upon the principle followed in the farm-loan acts of Congress where the profits arise from a percentage of the investments or loans made. In fact, this act was itself based upon such business long carried on prior to the act, and the relation of capital to that investment is also followed in the amendments proposed and as concretely evidenced in its application to our own corporation.

It is clearly evident that the proposed law did not have a business of this character in any of its provisions, and any attempt to make an application of it is practically impossible; therefore, in justice to it the special provision proposed should be made.

If we are left to the uncertain provisions of the bill as drawn, the total tax under the bill will be over \$36,000, as upon the price paid for this stock in the last sale for cash the present holder would have no income derived from his investment for the reason that the exemption allowed of 8 per cent upon the fair value of the capital miscarried in this particular business.

PEARSONS-TAFT LAND CREDIT CO.,

By OREN B. TAFT, *Vice President*.

The CHAIRMAN. The committee will now proceed to executive business.

(At 12 o'clock m. the committee went into executive session.)

APPENDIX.

During the sessions of the committee the following briefs were received and by direction of the chairman were ordered printed in the record, as follows:

BRIEF IN REGARD TO SECTION 900.

TAPESTRIES AND TEXTILES FOR FURNITURE COVERINGS OR HANGINGS FOR INTERIOR DECORATIONS.

This is general and the intent of the paragraph is not clear. It would cover cheap curtains and curtain materials which are house furnishings and are used by the poor, as well as the rich, as a comfort and necessity for the home. Our contention is that these articles should properly be placed in section 905 as, above a certain price, say \$2 a square yard and \$7.50 a pair at retail, they become luxuries and should properly pay a luxury tax of the amount your committee may name.

If the impost of 10 per cent on manufacturers, importers, and producers were to remain, the sale of this article would so decrease that the revenue would be smaller than could be collected in section 905. The income of the manufacturers would become a loss, and therefore the income tax would suffer, and an impending gross-sales tax would also become smaller. The larger revenue can only be procured by the 20 per cent tax collected by the vendor from the purchaser. We have submitted in a former letter the British luxury list, and if you will see the French list now in force you will also find an exemption up to a certain price on curtains and materials.

Furthermore (see 900) these goods are sold on 70 to 90 days' time, and it would be a great hardship for manufacturers to report monthly to the collector when payment is made, sometimes in three to six months. During the last famine hangings proved a great boon. They kept out the cold and soot.

We therefore ask you to kindly make this change.

Respectfully submitted,

CURTAIN MANUFACTURERS' ASSOCIATION OF AMERICA,
M. E. WORMSER, *President*.

UPHOLSTERY GOODS AS AN ESSENTIAL.

The Anthracite Coal Operators' Association, under date of September 4, advises that "householders who would conserve their coal supply and make their houses warmer should use heavy draperies for doors and windows."

It is a very practical suggestion.

From the earliest period, rugs and tapestries have been used in the finest old castles of Europe, primarily to check drafts; if they possessed an esthetic value, so much the better. But to-day, with the price of coal so high and the supply limited, it is pleasant to feel that such practical people as the coal men recommend the use of drapery stuffs as contributing to the comfort of the home. We are too prone to dwell upon the unessential qualities of estheticism in house furnishings, because comfort is an all-desirable quality, but there's no comfort so great as warmth in blizzard weather; so it might be well for dealers in their advertising to dwell upon the recommendation of the coal men.

FRENCH TAX ON LUXURIES.

Law enumerating articles subject to tax of 10 per cent on retail sale price.—The French finance law of December 31, 1917, by article 27 instituted a tax of

10 per cent on the retail sale price of luxuries. The Journal Officiel of March 24, 1918, published the text of a law, promulgated March 22, enumerating the articles which are classed as "de luxe." All payments of less than 1 franc are exempted from the tax, provided always that the payments are not on account of a larger sum. For the purpose of calculating the tax a fraction of a franc is deemed to be 1 franc. Rules are to be issued laying down the exact manner in which the tax will be applied. The tax was to take effect three months after the promulgation of the above-mentioned finance law, i. e., three months from December 31, 1917.

Articles taxed irrespective of price.—The following articles are submitted to the tax by reason of their nature, no matter what their price may be:

- Photographic appliances, lenses, and accessories.
- Motor vehicles for the transport of persons, their framework (chassis), and carriage-making materials and accessories (carrosserie).
- Jewelry of gold or platinum.
- Billiard tables and accessories.
- Hosiery and underwear (lingerie) of silk, pure or mixed.
- Artistic bronze work, ironwork, and locksmiths' work (serrurerie).
- Horses, ponies, asses, and mules for pleasure purposes (de luxe). (Breeders are not liable to this tax.)
- Curiosities, antiques, and all objets de collection.
- Brandy, liquors, aperitifs, and liquor wines.
- Sporting guns, hunting and sporting articles, and ammunition and accessories (armurerie).
- Live game for hunting or restocking coverts.
- Harness for saddle horses.
- Fine jewelry.
- Books (librairie); artistic publications on special paper with a limited impression.
- Livery (of domestics, etc.).
- Watches of gold or platinum.
- Goldsmiths' and silversmiths' ware (orfevrerie) of gold, silver, or platinum.
- Perfumery (rouge, scents, essences, extracts, etc.), excluding soaps and dentifrices.
- Paintings, water colors, pastels, drawings, and original sculpture. (Original works in this category sold direct by the artist are exempt from this tax.)
- Fine pearls.
- Pianos, other than upright (cottage) pianos.
- Precious stones and natural gems.
- Tapestry, ancient or modern, in wool or silk, machine or hand woven; oriental carpets; bathroom carpets (tapis de savonnerie).
- Truffles, truffled poultry and game, and truffle patties.
- Hunting garments and riding habits.
- Pleasure canoes and boats with mechanical propulsion, yachts.

Articles taxed above specified prices.—The following articles are taxed when the retail price exceeds the price in francs per piece indicated:

Lamp shades.....	10	Hosiery, underwear (lingerie de corps):	
Men's and women's clothing accessories.....	10	Children.....	20
Pets (animaux d'agrement):		Men.....	40
Dogs.....	40	Women.....	40
Other animals.....	10	Brushes, combs, and other toilet articles.....	10
Articles of furniture and accessories.....	10	Frames (for pictures, etc.).....	10
Articles de Paris, fancy or oriental articles of all kinds other than those comprised in the above schedule.....	10	Walking sticks, hunting stocks.....	10
Fancy articles for office use.....	10	Chinaware:	
Smokers' requisites.....	10	Table service for 12 persons (about 116 pieces).....	200
Devotional articles.....	10	Small single pieces.....	2
Bicycles.....	250	Medium size pieces.....	5
Silver jewelry.....	10	Large pieces.....	15
Imitation or rolled (double) jewelry or jewelry made of nonprecious materials.....	10	Complete toilet service.....	30
		Single pieces.....	10
		Tea or coffee services.....	30
		Single small pieces.....	2
		Large pieces.....	10

Men's headwear.....	20	Household linen:	
Women's hats.....	40	Tablecloths.....	60
Footwear, per pair:		Pillowcases.....	10
Children.....	25	Tablecloths, napery, by the	
Women.....	40	square meter.....	15
Men.....	50	Table or toilet napkins.....	4
Chocolates, confectionery, bon-		All other articles.....	4
bons, per kilogram.....	8	Lustels, lamp brackets, chande-	
Corsets, belts.....	50	liers.....	100
Complete costumes or overcoats:		Trunks.....	100
Children's.....	80	Fancy leather goods (maroqui-	
Little boys' (garconnets)...	125	nerie).....	25
Men's (suits, frock coats,		Furniture:	
morning coats).....	200	Bedroom, drawing-room,	
Complete suits (veston) for		dining room, study, for	
men.....	175	the whole and for each....	1,500
Separate garments:		By the piece—	
Waistcoat.....	25	Small.....	100
Trousers.....	50	Medium.....	250
Coat, smoking jacket, frock		Large.....	500
coat, morning coat.....	125	Looking-glass articles (miroir-	
Jackets.....	100	terrie):	
Costumes or mantles:		Mirrors.....	20
Young girls'.....	150	Picture-frame glass.....	100
Women's.....	250	Motorcycles, side cars, cycle	
Separate garments:		cars, and similar vehicles....	2,000
Skirts.....	100	Watches, other than those com-	
Bodices (corsages).....	80	prised in the above schedule..	50
Blankets, quilts, elder downs		Handkerchiefs, per dozen.....	18
(edredons).....	100	Ornaments and knick knacks....	10
Cutlery, scissors, each article...	10	Goldsmiths' and silversmiths'	
Lace, embroidery:		ware (orfevrerie) in base	
By the metre—		metal, plated (gold, silvered,	
Machine made.....	2	etc.), with the exception of	
Handmade.....	10	table ware, per piece.....	15
By the piece—		Umbrellas, parasols, sunshades..	25
Machine made.....	6	Perfumery; articles other than	
Handmade.....	30	those comprised in the above	
Fans.....	10	schedule:	
Artificial or sterilized flowers,		Soap, per cake.....	2
each purchase.....	10	Dentifrice, per liter.....	15
Natural flowers, conservatory		Toilet preparations contain-	
and indoor plants (de serres		ing alcohol.....	15
ou d'appartements), each pur-		Feathers, etc., for ornamenta-	
chase.....	10	tion (parures en plumes).	
Furs (fourrures). (See Furs		(See Ornamental grasses and	
below).....	100	feathers below).....	25
Gloves, per pair.....	8	Clocks (wall variety, etc.). (See	
Fire irons.....	100	Alarm clocks, etc., below)....	100
Engravings, prints, photographs,		Furs (pelletteries). (See Furs	
and reproductions of works of		above).....	50
art.....	100	Photographs:	
Gaiters, leggings, per pair.....	30	Portraits, per dozen.....	40
Accessories for games and		Enlargements, each.....	40
sports.....	25	Upright (cottage) pianos and	
Fishing tackle.....	10	harmoniums.....	1,200
Musical instruments other than		Ornamental grasses and feathers	
the piano (phonographs, gram-		(plumes de parure). (See	
ophones, mechanical pianos)		Feathers, etc., for ornamenta-	
and all their accessories.....	150	tion above).....	10
Binoculars (opera, racing, etc.)		Alarm clocks, traveling clocks,	
and lorgnettes.....	30	desk clocks. (See Clocks	
Games.....	20	above).....	20
Lamps, candelabra.....	50		

Curtains, bed curtains, and fittings for same, French windows:		Carpets—Continued.	
Per curtain or curtain fitting	100	Ordinary carpets fixed by nails (tapis cloués), the meter (1 m. by 70 m.)	20
Door curtains, double	100	Ordinary carpets of large size	25
Door curtains, single	60	Table covers, bedspreads	80
Bed decorations	50	Tissues for clothing or furnishing, the square meter	20
Window curtains, short window blinds (brise-bise), per pair	30	Mural hangings of all kinds, per square meter	5
Bound books (reliure), each volume:		Clothing for the house (vêtements d'appartement), peignoirs, pajamas, dressing gowns	80
In octavo and smaller formats	10	Portmanteaux, traveling bags	75
In folio and quarto	20	Glassware and crystal ware:	
Ribbons, braids, etc. (passementerie), per meter	5	Large glasses	2
Ladies' bags	40	Small glasses	1½
Saddlery:		Glassware for toilet or office use	10
Complete harness for carriage	600	Large articles, carafes, jugs, and such like	10
Single pieces	150	Wines:	
Window accessories (stores de vitrage ou de fenetre)	50	In bottles	5
Articles in imitation bronze	10	In casks, per liter	3
Carpets:		Horse carriages for private use	1,000
Center carpets	100	Aviaries, cages	10
Beside mats and hearth rugs	25		

The Journal Officiel of April 6 publishes a law, promulgated on April 5, providing that payment for goods bought before January 1, 1918, are exempt from the above-mentioned tax.

In France a commission was appointed to decide upon the articles which should be subject to the tax on luxuries, just as a select committee of the House of Commons has been appointed for a similar purpose in England. The chairman of the French commission, in reporting to the French minister of finance, outlined the commission's procedure, as follows:

"It would have been vain to attempt a rigorously exact definition of objects called luxury objects. Besides, Parliament has not given us a mandate to undertake a theoretic study, but to furnish it with concrete propositions with a view to the classification called for by the law of December 31, 1917.

"This is not to say that in order to draw up these lists we have not been guided by certain principles. We judge that the quality of luxury articles depends on three elements—the nature of the article, its price, and its destination.

"In the first category are included articles which are essentially de luxe, such as diamonds, pearls, jewelry in gold or in platinum. In the second, objects which in a general way are in everyday use, such as clothing, but which are of a sumptuous character, when they fetch high prices. Finally, certain articles which are de luxe by nature, such as motor cars, lose this character when they are employed in the exercise of a profession; for example, the furs of a chauffeur or the carriage of a doctor. The law, indeed, is intended to hit only the display of wealth and not the instruments of labor; it taxes luxury but does not wish to paralyze effort.

"In this light we were led to the drawing up of three schedules; the first, comprising luxury objects by nature; the second, objects classed by reason of their price; the third, exemptions accorded to certain articles by reason of their destination.

"After some hesitation the commission decided that it was expedient to draw up only the first two schedules, at the same time indicating in their heading the principle of derogation founded on professional use.

"The first difficulty that the commission had to grapple with in the drawing up of the schedules A and B consisted in making a classification as complete as possible, with designations sufficiently clear to avoid all difficulties in application. In this matter we thought we could not do better than to follow the customs of the trade; it is traders who will be, in the application of the law, the

principal collectors of the tax; it was necessary, therefore, to make our schedules conform to their traditions and their customs. The categories proposed by the commission are presented with the concurrence of the representatives of trade; if some designations appear to the public obscure or incomplete, the purchaser will be enlightened at the time of payment by the seller of the article upon which the tax is levied.

"The question of fixing the price above which certain articles will be considered as being de luxe occupied for a long time the attention of a subcommittee and the commission itself.

"We must observe that the figures given in Schedule B represent current prices (les prix actuels); since it concerns a tax to be collected at once, and, since we take price as the test of luxury, it could only concern the present price paid (prix actuellement paye) for each article. The result of this has been that in a large number of cases we have allowed exceptional figures, clearly higher than those ruling for purchases before the war. It will evidently be necessary to proceed with a revision of these basic prices (prix de base), when the market, so profoundly disturbed by the rise in cost of labor and raw materials, resumes its normal state.

"A very important question, and one which may have a serious reaction on the yield of the tax, has been settled by the heading of schedule B; it is there stipulated that the tax is due not by reason of the sale price but only by reason of the excess of this price over the basic price appearing in the schedule. This solution appears to satisfy the demands of equity and to accord with the conception of luxury which we have indicated above; up to a certain price the purchase of a piece of furniture, of an article of clothing, corresponds to a real need; luxury, and consequently the tax, only ought to begin above that price. Nothing in the text of the law of 1917 is contrary to this interpretation, and this is supported by a recent precedent, since this rule has served as the basis of the assessment of the lump-sum tax on income.

"The question of the derogations justified by professional custom was very delicate and would have given rise to long enumerations if we had wished to enter into details of all kinds; we have thought subsequently that it was preferable to fix by a general formula the principle of exemption for articles destined for the public services, agriculture, commerce, industry, and the exercise of a profession. But this rule, laid down as a hard and fast one, would have led to excessive indulgence if certain exceptions were not made to it. Thus the doctor of whom we have spoken above may have need of a motor car to visit his patients; but he has no need of a very luxurious carriage, and above a certain price he ought to pay the tax. In this and other similar cases, we have introduced in the schedules A and B certain precise definitions which will secure that the exemptions, which taken in themselves are just, do not lead to abuse."

TAX ON ATHLETIC GOODS.

NEW YORK, September 18, 1918.

HON. F. M. SIMMONS,

Chairman Finance Committee of the Senate,

Washington, D. C.

DEAR MR. SIMMONS: I take the liberty of addressing you as chairman of the Finance Committee, suggesting certain changes in the administrative features of the tax levied under Title IX of the proposed war-revenue bill recently passed by the House of Representatives and now before your committee for consideration, especially to the tax proposed by section 900 on sporting goods.

While I think the remarks which I shall make are general in their application to all the articles enumerated in section 900 where the tax is imposed on the price at which the articles are sold by the "manufacturer, producer, or importer," nevertheless it must be understood that I am writing only as a business man interested as an officer of A. G. Spalding & Bros., athletic goods manufacturers, in the production and sale of athletic goods including bathing suits, one of the new items subjected to the tax by said section 900.

At the time of hearings held a little over a year ago by your committee on the war-revenue act of October 3, 1917, I had the honor of appearing before your committee, testifying in opposition to any tax on athletic goods. When the present bill was being considered by the Ways and Means Committee of the House I had extended to me the privilege by that committee of appearing be-

fore them, and the testimony and proof which I presented there is printed in full in the Hearings before the Ways and Means Committee on the New Revenue Bill under date of June 8, 1918, appearing on pages 57 to 78.

While I presented at that time what appeared to me to be valid arguments against the imposition of an excise tax on athletic goods, the Ways and Means Committee have decided otherwise, and while I still hold the opinions therein expressed, the whole subject of this particular section of the tax law is of such relatively little importance that I believe it is wiser not to press before your committee any further arguments in opposition to the tax itself or to the rate which has been selected by the House of Representatives. The suggestions, therefore, that follow have as their object to make the meaning of the law somewhat clearer, to eliminate certain inequalities between different manufacturers, producers, and importers, which I believe would exist if the law was passed in its present form, and while accomplishing these two results at the same time increase slightly the total tax to be collected without any change of the rates which are embodied in the proposed law.

I believe that no one will dispute that this tax is in principle a consumption tax. It is a tax which Congress presumes will be passed on and borne ultimately by the consumer of the taxed articles. From this it follows that the tax should be equal on identical articles sold to the consumer at identical prices, or, to put it negatively, that such articles should not be subject to a different amount of tax according to the method or means of distribution used by the manufacturer, producer, or importer to distribute his goods to the consumer. It would seem that the Ways and Means Committee had this in mind by the language they used in section 901 and by the following clause which is inserted at the end of section 900:

"If any manufacturer, producer, or importer of any of the articles enumerated in this section (900) customarily sells such articles both at wholesale and at retail, the tax in the case of any article sold by him at retail shall be computed on the price for which like articles are sold by him at wholesale."

It is respectfully submitted, however, that section 901 and the above-quoted clause of section 900 does not accomplish the result which it is presumed was intended.

The manufacturer, producer, or importer may use three methods for distributing his merchandise:

1. He may sell direct to the consumer.
2. He may sell direct to the retail trade (meaning by "retail trade" the stores which sell to, or the major portion of whose business is with the consumers).
3. He may sell to jobbers or large distributing houses who in turn resell to the retail trade.

It is understood, of course, that there may be many subdivisions within these three general classes, and that the manufacturer does not always use any one of the three methods exclusively, but may use a combination of two, or sometimes all three methods.

There is no such thing as a market price for articles of commerce such as are listed in section 900. The price which the manufacturer will charge will differ very materially according to whether he is selling direct to the consumer or direct to the retail trade, or to a jobber or distributor. Without going in detail into the business economics which underlie and justify this difference in price it is sufficient, perhaps, to say here that the amount of capital required and the expense involved increase as the manufacturer tries to approach closer to direct relations with the ultimate consumer. Furthermore, where the manufacturer sells direct to the consumer he almost always has one fixed price from which he never makes any concession. The same is very largely true where the manufacturer sells direct to the retail trade; where, however, we find a manufacturer dealing with jobbers and distributors, there is a tendency to enter into individual contracts, and the prices to the different jobbers and distributors tend to vary.

The Ways and Means Committee very evidently intended that the tax should be on the price at which the articles manufactured are sold to the retail trade, but the language used does not give effect to this intent probably because the committee was not entirely familiar with the actual trade conditions.

Section 901, I think, would lead to an endless amount of dispute and probably to much expensive and wasteful litigation between taxpayers and the Treasury Department, for the following reasons:

First. There is no way of determining what is the fair market price obtainable for any particular article. As stated above, there is no such thing as a market price for articles enumerated under section 900.

Second. The phrase "directly or indirectly to benefit such person or any person directly or indirectly interested in the business of such person" is ambiguous and almost impossible of being given any precise meaning.

No price concession is ever made in a bona fide trade transaction that is not intended to at least indirectly benefit the seller, and yet it would always be doubted whether Congress intended that language to have as broad a meaning as that.

I would respectfully suggest that section 901 be omitted entirely in its present form; that the following changes be made in section 900 and a new section 901 inserted in the language given below.

In place of the following language in section 900: "A tax equivalent of ten per centum of the price for which so sold," insert the following: "A tax equivalent of ten per centum of the wholesale price for which such articles are customarily sold to the retail trade by such manufacturer, or by the distributors or jobbers to whom such manufacturer has sold."

In place of the following clause in section 900: "If any manufacturer, producer, or importer of any of the articles enumerated in this section (900) customarily sells such articles, both at wholesale and at retail, the tax in the case of any article sold by him at retail shall be computed on the price for which like articles are sold by him at wholesale." insert the following: "If any manufacturer, producer, or importer of any of the articles enumerated in this section (900) sells such articles only at retail, the tax in the case of any articles sold by him at retail shall be computed on three-fourths of the price for which so sold."

The way the law is drafted at present a manufacturer who sells only at retail (and, so far as I know, there are none such in the athletic-goods trade, except golf and tennis professionals) would have to pay a tax on the full retail price. This is not fair to him because he necessarily is paying a larger tax on this same article, selling to the consumer at the same price that his competitor has to pay who distributes his goods by some other method. Where the manufacturer sells only at retail it would be difficult, if not impossible, to determine what the correct wholesale price to the retail trade for such merchandise is, there being, as I have stated, no such thing as a market price for merchandise of this kind. I think it is safe to say that in any line of trade the average wholesale price to the retail trade of any article of the class of those enumerated in section 900 varies from 60 per cent to 75 per cent of the retail price. The number of manufacturers who sell direct to consumers only and do not sell at all to the retail trade, I think, will be found to be very small in any of the trades enumerated in section 900, and hence it seems fair to those few that the percentage of the price on which the tax should be computed should be taken at the highest average rather than the lowest average. In the place of the present section 901 I would suggest the following:

"SEC. 901. That there shall be no change in the price on which the tax is computed by reason of any cash, quantity, or trade discount, unless in the case of a trade discount only such trade discount be allowed to all the retail-trade customers of such manufacturer, producer, or importer. The intent being that the tax on any given article of the manufacturer, producer, or importer shall not be varied by the special terms of any particular sale or contract of sale."

There is one other matter which I would like to submit for consideration to this committee, namely, the question of tax on articles enumerated in section 900 which are sold to the Y. M. C. A., Knights of Columbus, and other organizations for the use of the Army and naval forces of the United States. The Commissioner of Internal Revenue has ruled that pursuant to the provisions of section 3404 of the Revised Statutes of the United States, sales to the Red Cross are not subject to the present excise tax imposed under section 900 of the war-revenue act of October 3, 1917, because the Red Cross is in effect a department of the Government itself. Their present rulings with respect to the Y. M. C. A., Knights of Columbus, and other organizations have been, up to the present time, to the contrary, although I believe the matter is now being pressed by the Y. M. C. A. to secure a similar ruling in their case to that of the Red Cross.

So far as our company is concerned, it is indifferent to us what Congress does in this matter. If the tax is imposed, we, of course, will have to collect it from

the organizations purchasing merchandise from us, and if there is no tax they will buy at correspondingly lower prices. If the law is passed in the form such as I have suggested, or probably even in the form as it now stands, the price will be more than 10 per cent of the price at which such organizations as the Y. M. C. A. and Knights of Columbus are purchasing, because they are purchasing in very large quantities and are receiving and are entitled to receive the prices at which the manufacturer would sell to the Government itself or to large distributors, and which, of course, are very much less than the regular wholesale prices to the retail trade. It is therefore respectfully submitted that Congress should make this subject clear and unambiguous by expressly exempting sales to all organizations who are furnishing goods for the use of the Army and Navy. With this in view I submit the following section, which I have numbered section 901-A, for this purpose:

"SECTION 901-A. That under such regulations as the Secretary of the Treasury may prescribe all articles enumerated in section 900 shall be exempt from the tax imposed by said section 900 which are sold to the United States, and when for the use of the Army and naval forces of the United States which are sold to the American Red Cross, the Y. M. C. A., the Knights of Columbus, and any other organization which the War and Navy Departments will certify are bona fide furnishing such articles to the Army and naval forces of the United States."

Respectfully submitted.

H. BOARDMAN SPALDING.

*Vice President and Treasurer of A. G. Spalding & Bros.,
126 Nassau Street, New York, N. Y.*

Tapestries and textiles for furniture coverings or hangings in the interior decorations of buildings, 10 per cent tax.

Carpets and rugs, an amount in excess to \$5 per square yard, also subject to tax.

Comparison: These two clauses, in our opinion, it is the Government's intention to tax in about the same way, as they are used under the same circumstances and both come under the heading of interior decorations. The second item carries a tax which evidently is meant to show some consideration to the general public, who all use this product when sold at prices the average civilian can afford for his home.

In the first item there is no consideration shown at all to the users of staple goods against the users of luxuries, although there should be more consideration given to the first than to the second, for the reason that tapestries and textiles cover a much greater scope than carpets and rugs.

Textiles may mean all classes of cotton goods, whether printed or not. Printed textiles are, as you know, used for the cheapest kind of clothing, such as children's dresses, aprons, women's wrappers, kimono's, etc. Some manufacturers of printed textiles call their goods cretonne, because they specialize in selling the trade who in turn supply the house furnishers, and it is generally understood that a piece of printed cloth used for the interior decorations of a building is called cretonne.

Therefore a manufacturer of cretonne is in a general way understood to sell his product for the interior decoration of buildings, and under this heading will be taxed, although he is constantly selling his product to manufacturers in all branches of trade, and in many cases sells as much for general usage as he does for decoration. Under the circumstances, how are you to tax the product which does not go into the interior decoration of buildings? For instance, a manufacturer who makes printed percales, awnings, denims for overalls as well as for draperies, silkoline for quilts, satines, calicoes, trunk linings, gingham's, or any other printed piece of cloth who sells his product, and then in turn it is used later on for interior decorations—how is he going to be taxed under this law, although the goods are exactly the same as the goods made by the cretonne manufacturers. Because he calls his product by another name, should he escape this tax? It is quite clear that this tax as it is written now does not convey the Government's intention.

There are enormous quantities of burlap used for the covering of walls of buildings which will be subject to a tax of 10 per cent. How are you to separate this from the burlap used for packing and other purposes?

To avoid complications, which will surely arise, and to make this a workable tax, we would suggest that a price be set on tapestries, drapery textiles,

drapery nets in the piece or pair of \$1.50 per square yard. This would be, in our estimation, more nearly the original intention the Government is working for.

During September, 1918, one of the requests from the Fuel Administrator was that people should draw their draperies at the doors and windows during the cold weather, and particularly mentioned the drawing of these draperies in unoccupied rooms. We quote this to show further utility use of draperies.

DEERING MILLIKEN & Co.

TITUS BLATTER & Co.

ALEXANDER JAMIESON & Co.

CONSUMERS' PURCHASE TAX.

Whether or not it will be necessary to raise for governmental purposes the vast sum of \$24,000,000,000 or more, I certainly do not pretend to know or question. But whether the amount to be loaned to our allies should in part be paid for by direct tax on our citizens or not, is to me one of grave doubt. As I understand it, our Government takes the bonds of our allies for these loans, and if so, should we not sell our Government bonds to our citizens to raise this money, rather than tax our citizens for any material part of it? When a citizen pays a tax it is forever gone from him; but if he buys a bond he has simply loaned his money; and as our Government is simply loaning this money to the foreign Governments and taking their bonds, it looks to me reasonable for them to likewise borrow the money from our citizens on its bonds.

Considering this feature, is it wise or prudent at this time to try to raise one-third of the total amount to be expended by the Government, including foreign loans, by taxation, amounting to, say, \$8,000,000,000? Can the business of the country continue to stand the heavy strain of taxation as now proposed, and at the same time buy and consume the amount of bonds necessary to produce the other two-thirds of the revenue needed? It makes no difference how abundant or prolific a milch cow may be, you can milk her dry, and though leaving the body of the cow intact and not harmed, you have then taken from her all that she can give of what you want. It is well to remember, too, that not all of the cows in the herd give milk, but a greater proportion of them give it than there are people in the United States who pay direct taxes to the Federal Government. I think it was estimated last year that only about 3 per cent of the total population of the United States paid any Government tax. Therefore, approximately 100,000,000 people were enjoying the benefits and protection of this Government, without its costing them one cent. Now, no man is liable to appreciate very much anything which comes to him without care or effort.

If it be necessary to raise anything like \$8,000,000,000 by taxation, are there not other ways than those now proposed, by which a very considerable portion of this tax could be raised, and not bleed to death the very small proportion of the people now paying direct taxes (say, 3 per cent), and put them in such condition as that they can not continue to respond to the various calls of the Government?

Therefore I want to suggest a form of taxation not now in existence, but which the needs of the Government appear to me to necessitate, simply and entirely as a war measure. This method of taxation is what would properly be called a consumer's purchase tax. A reasonable proportion of the whole taxes of the country could readily be raised by a tax of this kind, and no unreasonable amount should be raised by it. It is the only method of taxation that I know of that every consumer would pay a portion of, and a portion based entirely on the amount consumed. If a man's consumption was small, he would pay but little; if his consumption was large, his tax would be proportionately heavy. No one could easily evade it, and everyone, under the present needs of the Government, should be willing to pay something directly toward the maintenance of the Government. It would be paid day by day, as purchases were made. It would not be a particular burden or hardship, and would produce a large revenue, governed, of course, by the amount of per cent taxed against the purchase.

In no way could it be made a debt-producing obligation. At the time of the purchase the consumer would pay the tax, be it 2 cents or \$5.00. The poor man, earning a livelihood by the sweat of his brow, would hardly miss from

his daily wage the amount required for this tax. If he spends \$600 a year, and the rate does not exceed 5 per cent of the amount of purchase he would make, and the class of materials he would consume, it would hardly cost him more than \$30 per annum, or, say, 1 to 1½ per cent of the total number of working days in the year under the existing scale of wages. I think there is no man who is deserving of citizenship who would not be willing to make this sacrifice, if sacrifice it can be called, to help support his Government under present conditions.

While, as I said above, this tax would apply to all, and everybody would be doing something, it would still largely be paid by the rich man, or the man who has another income besides his daily wage. This tax is not "giving until it hurts," but it is giving to the man who pays it a direct interest in his Government, and makes him a more manly man. It makes him feel that he is part and parcel of the Government and equally deserves with all other citizens the cure and protection which the Government can and does give.

The consumers' purchase tax is in no sense class legislation, but makes one class of all. We neither want nor need class legislation in war times for the support of the Government. The rich and the poor alike are fighting in the trenches, side by side, each doing his whole duty. Then, why not everybody, by this purchase tax, pay a portion of the taxes necessary to support our soldiers.

A tax on luxuries (if anyone knows what are luxuries at this time) is distinctly class legislation or class taxation; if confined to articles enumerated as luxuries, and therefore, in my opinion, does not meet the needs of the Government under existing conditions. Under this proposed consumers' purchase tax, what might be called luxuries would certainly carry a very high tax. This tax could be so graded that where the purchaser wanted to make a purchase costing \$1, he would pay one rate of taxation, and where the consuming purchaser wanted to make a purchase of \$500 or \$1,000, he would have to pay a very different rate of taxation. This would be fair to all. One need not pay a high consumers' tax unless it suited him to do so.

This tax would teach conservatism and economy, and to purchase only such things as were, so to speak, needed or necessary. It would discourage useless expenditures. At the same time it would produce a revenue astonishingly large.

Being paid day by day, it would not disturb the financial situation, as is now necessarily done by the collection of the enormous income and war profits taxes. I do not mean by this that either of these taxes ought or should be abolished. They are absolutely necessary, and if unreasonably severe, no one ought to complain at having them to pay. This consumers' purchase tax would simply be an adjunct to taxes collected in other ways, and would not be intended in any way to be substituted for them, though it might enable some reduction in these taxes where it is found they are oppressively heavy and working material injury to the business of the country.

During the Civil War there was proposed several times in Congress a tax known as a sales tax, but in each instance it failed of passage, and it is readily understandable why such a bill could not pass and would not be proper to pass under the present war conditions. As I understand it, the bills then offered taxed every sale. When a manufacturer sold goods to a jobber, the jobber paid a tax; when the jobber sold it to a smaller jobber, the small jobber paid a tax; when that small jobber sold it to the retailer, he paid a tax; and when the retailer sold it to the consumer, he paid a tax. So there was piled up three or four taxes on the article when it came to the consumer, which was tax on top of tax, so that it almost amounted to prohibition on general business. But the consumers' purchase tax herein suggested would not interfere with business in any sense as it is now being carried on. In fact, the business world would hardly know there was such a tax. The manufacturer would pay no tax when he sold any goods. The jobber would pay no tax. The retailer would pay no tax; and the only person paying a tax would be the consumer when he paid for the article. It would be only one tax, and that a small one, unless, as heretofore stated, the purchaser wanted something that might be called a luxury, and the purchase of which involved a considerable sum of money.

It also has the advantage of being a tax easily and cheaply administered and collected. It could all be done by putting the necessary stamps on the article purchased, these stamps to be paid for by the purchaser, of course. The retailer could go to the revenue office or post office and buy an assortment of

these stamps, and when the article was sold inform the purchaser the amount of tax he would have to pay and sell him the stamps to apply to the purchase. Such safeguards and regulations could be enacted as would make the law easily administered, all the details of which could be carried out, it appears to me, as thoroughly and as well as is done now by the Internal Revenue Department or the post office in selling stamps.

It appears that some other source of revenue must be found to meet the needs of the Government, unless the business of the country is taxed to a point which might materially interfere with it, and also impede to some extent the ready sale of the enormous amount of bonds which the Government is compelled to dispose of.

It has been intimated by one high in financial authority that the politicians would not approve a bill of this character. I suppose, of course, the politicians here referred to are Members of Congress, because only the Members of Congress would have anything to do with the passage of such a bill. I had learned to think that there was no such thing as politics in Congress, where the welfare and necessities of the Government and the proper prosecution of the war was concerned; that Congress had virtually "pooled" its politics when it came to matters of that character, just as I understand the Army has pooled religion in the different cantonments, and have put all the religion in one pot, so to speak, virtually saying that the soldiers had just as well go to Heaven in the sprinkling cart of the Presbyterians as in the submarine of the Baptists.

If one-third of the people of the United States paid this consumers' purchase tax (and it seems reasonable to suppose that that many would have to pay it), and the average amount paid by each was \$33 per annum, it would produce a tax of over a billion dollars, and this enormous sum could be produced by this consumers' purchase tax without embarrassing or doing violence to anyone.

In the language of ex-Speaker Cannon in a recent interview: "In such a dilemma why not adopt a consumption tax?"

Respectfully submitted.

S. T. MORGAN.

RICHMOND, VA., September 18, 1918.

THE NEW WILLARD,
Washington, D. C., September 19, 1918.

Hon. F. M. SIMMONS,

Chairman Finance Committee, United States Senate.

MY DEAR SIR: A brief of my suggestions in regard to a change in section 900, paragraph 15, and section 905, paragraph 1, affecting rugs and carpets, is herewith submitted for your committee's consideration:

Oriental as well as other imported rugs have so greatly increased in their cost as to make the proposed tax, unless changed, almost prohibitory. The cost of such rugs has reached a high level undreamed of before the war, due to the following reasons:

- (a) Large increase in their price abroad.
- (b) Fifty per cent duty on such increased foreign cost.
- (c) Increase in the cost of ocean transportation and marine insurance.

When to these factors is added the great increase in the overhead cost of operation of any business in this country, a rate of taxation approximating 20 per cent on the selling price of an article possessing in a high degree utility and art is bound to result in the disorganization of business and consequent failure to produce the maximum revenue possible from this source.

There is always a limit at which any article can be sold, and to impose a tax excessively on its selling price without regard to the profit that is possible to make on such a sale is very different from taxing the net profits at howsoever high a rate.

Modern imported rugs can scarcely be sold at retail under \$3 per square foot, or \$27 per square yard. Ranging from that price, they run up to \$10 per square foot, or \$90 per square yard. An allowance of \$3 per square yard on these would still leave a net tax of 16 per cent to almost 20 per cent.

A large percentage of the rugs manufactured in this country also sells at a price in excess of \$15 per square yard.

The change herein suggested includes such American rugs, thus placing them at no disadvantage.

Likewise by excluding imported and American rugs in section 905 and leaving the \$5 exemption on all other carpets and rugs the purposes of your committee would be fully served by giving the intended benefit to the low-priced goods.

The pending bill provides in section 900, paragraph 15, and section 903 a flat tax of 10 per cent on the sale price of artistic interior furnishings and other objects of art and of decorative value—all articles sold under like conditions and associated with high-grade rugs. The latter should, therefore, be included in this section.

As it is likely that this revenue bill will remain on the statute books for a considerable period even after the war, it is most essential that not only an injustice be prevented but also the largest amount of revenue possible be secured for the Government, and it will not be difficult to show to your committee, if necessary, that a straight flat 10 per cent tax, as suggested herein, will produce more revenue for the Government than could otherwise be obtained.

Respectfully,

S. KENT COSTIKYAN.

[Form of suggested change.]

TITLE IX. EXCISE TAXES.

Section 900 (15) to read: "Tapestries and other textiles for furniture coverings or hangings and imported and American rugs (made principally of wool and seamless) used in interior decorating and furnishing of buildings, 10 per cent."

Section 905 (1) to read: "Carpets and rugs (excepting imported and American rugs, seamless and made principally of wool), including fiber, on the amount in excess of \$5 per square yard."

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